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Applicant	: Kurt C. McCracken	Art Unit	: 3625
Serial No.	: 09/610,828	Examiner	: Nicholas Rosen
Filed	: July 6, 2000		
Title	: MANAGING INVESTMENT ASSETS		

Mail Stop Appeal Brief - Patents
Commissioner for Patents
P.O. Box 1450
Alexandria, VA 22313-1450

BRIEF OF APPLICANT ON APPEAL

Real party in interest

The real party in interest is Prana Fund Manager, LLC, a California limited liability company having a place of business at 665 Third Street, #450, San Francisco, CA 94107.

Related appeals and interferences

None.

Status of claims

All claims (1 through 29) have been rejected and are being appealed.

Status of amendments

No amendment was filed after the final rejection.

Summary of claimed subject matter

The invention relates to investment entities that acquire and manage properties for the financial and tax benefit of the entities' investors.

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In one example, consider individual investors who own small properties (for example, rehabilitated walk-up apartment buildings) and who would like both to diversify their holdings among a larger number of buildings and also to have a professional manager run the properties and decide when to buy, sell, and rehabilitate properties in accordance with an investment profile that is consistent with the investor's goals. For example, the profile may call for buying distressed properties in certain areas of a city, renovating them, and eventually trading them for other distressed properties. (specification, p.4, ll. 1-7)

In the example, these individuals first contribute their buildings to an investment entity in exchange for ownership interests in that entity. This contribution can be accomplished without the investor incurring a tax liability, while at the same time limiting the investor's legal liability (e.g., by holding a limited partnership, limited liability company, or corporate interest). This transaction also permits the investor to delegate the management and purchase, sale, and rehabilitation decisions to the managers of the investment entity in accordance with the profile. (p. 3, ll. 17-19, 28-29)

The investment entity then operates on behalf of its investors to analyze its properties against an investment profile, enhance some properties by physical improvements, and identify properties that are appropriate for disposition. Properties that are to be disposed can be traded for other properties in tax-advantaged exchanges. (p. 4, ll. 17-31)

The individual investor may continue to hold his interest, relying on the professional management of the investment entity, or may redeem his investment at its current value. (p. 5, ll. 5-6)

The investment entity thus holds a relatively large number of relatively small properties of a particular kind for the benefit of a relatively large number of investors, and permits the investors to acquire their interests in the entity through tax-free contributions, and later redeem their interests at current value.

To conduct such a business with respect to a large number of small properties that are bought, sold, improved, and traded in many transactions over a period of time, and to be able to redeem interests of any of the many investors from time to time at their respective current values,

the investment entity must perform complex computations using computers. (p. 4, ll. 8-15; p. 5, ll. 20-26)

The computers enable the tracking of each investor's basis (including book basis (for accounting purposes), tax basis, and fair market value basis), the allocation of that basis among properties of the investment entity (which change frequently), the continuing accounting for the resulting allocated basis and deductions, particularly depreciation, that results from a succession of tax-advantaged exchange transactions, and from time to time determining a current value of an interest in the investment entity based on characteristics of the properties held. (Id.)

By performing these operations, the investment entity is able to offer an investment interest to individual investors having characteristics that have never been available before in the combination contemplated by the applicant's invention.

These features and others are recited in the applicant's independent claims 1, 16, and 29, which all require that:

(a) properties are acquired from investors in tax advantaged transactions, in at least some cases as contributions in exchange for interests in the investment entity (p. 3, ll. 27-29),

(b) the value of at least one of the properties is enhanced by physical improvements (p.4, ll. 30 - p. 5, ll. 3),

(c) interests of the investors in the entity are redeemed at values based on the characteristics of at least one of the properties (p. 5, ll. 4-16),

(d) there is an investment profile for the entity's properties (p. 4, ll. 1-7),

(e) a property that falls outside of the profile is identified for possible disposition or is traded for another property in a tax-advantaged exchange (p. 4, ll. 17-21), and

(f) a machine (i) tracks each investor's basis in his interest, (ii) allocates the investor's basis among the properties, and (iii) tracks the allocated basis of each investor through a succession of tax-advantaged exchanges (p. 4, ll. 8-9, 17-29; p. 5, ll. 20-26).

The independent claims also recite features that differ among the three claims.

In claim 1, the machine also determines a current value of an interest in the investment entity based on characteristics of the properties and identifies at least one of the properties as appropriate for disposition. (p. 4, ll. 8-10, 27-29)

In claim 16, (a) the investment profile includes a disciplined portfolio approach that uses diversification and contingent risk minimization (p. 6, ll. 3-7), (b) the machine is also used to record and analyze investments held by the investment entity, to allocate the tax attributes of investments held by the entity among the investors, to track tax attributes allocable to each investor in the investments of the entity, and to analyze other properties against the investment profile for possible investment (p. 4, ll. 8-15; p. 6, ll. 24-28), (c) a management entity enhances properties held by the investment entity using physical improvements, refurbishment and management efficiencies (p. 3, ll. 30 – p. 4, ll. 1); and (d) there is a plan of redemption of interests of investors, the redemptions occurring at a value based on characteristics of one or more of the properties (p. 5, ll. 17-19).

In claim 29, (a) the exchanges of properties that fall outside the investment profile occur at a succession of different times; (b) the rate of redemptions of interests is controlled to reduce the need to divest properties at depressed values (p. 5, ll. 5-11); (c) each of the acquisitions and each of the redemptions is effected at the then current value of the interests of the investors based on the characteristics of properties held by the investment entity (*see* p. 5, ll. 20-26), and (d) the machine is used to track each investor's basis in his interest in the investment entity from his initial investment to a redemption of his interest (Id.).

<u>Grounds of rejection to be reviewed on appeal</u>

1. The rejection of each of the independent claims 1, 16, and 29 as having been obvious from what is described in Ward, "An Overview of Limited Liability Companies" and Hitchings, U.S. Patent Application Publication 2002/0143673, and a set of references (which were only cited for the first time in the final action and are listed in appendix B) said to constitute "official notice."

2. The rejection of each of the dependent claims as having been obvious based, in many cases, on no more than a mere assertion that the feature would have been "obvious" or

"well-known," without further explanation, without the citation of any prior art reference, and without any contention that there would have been motivation or suggestion to combine the feature with the features of the related independent claims.

Argument

1. The rejection of each independent claim as obvious from Ward, Hitchings, and the official notice was improper.

Claim 1

Of all of the features of claim 1, only a small portion were alleged by the examiner to be described in either Ward or Hitchings, namely (in the examiner's words), "acquiring one or more properties from one or more investors in exchange for an interest in an investment entity," (Ward), the "tax advantages of such investment entities (LLC's)" (Ward), "using a machine to (e) identify properties appropriate for disposition" (Hitchings), and "exchanging at least one of the identified properties that falls outside of an investment profile for at least one other property in a tax-advantaged exchange." (Hitchings) (Office Action of 4/28/2005 (OA), p. 4)

Other features of claim 1 supposedly fall within the rubric of official notice, namely the following features identified by the examiner: "managers/developers routinely enhance the value of property by physical improvements," "using a machine to (a) track each investor's basis in an investment entity, [etc.] is what mutual funds do," and "that late-20th century mutual funds with billions of dollars in assets, thousand of investors, and many complicated transactions, had used machines [computers] before the applicant's filing date, rather than employing large numbers of scriveners to make the necessary calculations on paper with quill pens." (OA, p. 5)

The examiner's rejection must fail for several reasons, most significantly because he has used the features of the claim itself in hindsight as a roadmap to piece together disparate features of a number of different references on a theory that this somehow would have made the claims obvious. To take that approach is not permitted by the law, of course.

The examiner has also not even asserted, let alone proven, that, as to at least some of the features that he pieces together with hindsight reasoning, there existed any suggestion or motivation to combine them.

Furthermore, at least some of the features of claim 1 are not the subject of any assertion at all by the examiner that they are found in the cited references (including in the official notice). In other words, not all of the features of each of the independent claims is alleged by the examiner to be found in any of the cited references (including the official notice).

For example:

1. The examiner asserts that Ward "discloses tax advantages of such investment entities (LLCs)" (OA, p. 4), but fails even to allege that Ward discloses what is actually recited in claim 1, namely that the properties are acquired from the investors through "tax advantaged transactions." The disclosure of "tax advantages of ... entities" by Ward, of course, does not amount to a disclosure of "tax advantaged transactions" as a way to get the properties from the investors into the entity. Thus, the examiner simply has not established that claim 1 would have been obvious from the prior art.

2. The examiner asserts by official notice that it was well-known and routine for mutual funds to "(c) track the allocated basis of each investor as a result of a succession of transactions." (OA, p. 5) Even if true, that notion is irrelevant to claim 1, because what claim 1 recites is tracking the allocated basis as a result of a succession of transactions that are "tax-advantaged exchange transactions." The examiner never even asserts that it was known or routine to do that, and has therefore failed to justify the rejection of claim 1 as having been obvious.

3. Although the examiner has asserted that Ward discloses acquiring properties from investors and discloses tax advantages of investment entities, that Hitchings discloses using a machine to identify properties for disposition and exchanging at least one of the identified properties, and that official notice implicates the existence of enhancing property values by physical improvements, redeeming an interest based on current value, tracking each investor's basis, allocating each investor's basis, and tracking the basis as a result of transactions, nowhere has the examiner said anything about any motivation or suggestion to combine these features to reach the invention.

At the heart of the matter, the examiner has catalogued certain features from two references, has alleged the existence of some features from official notice, and yet has made no assertion and given no evidence that combining any pair of those features or all of them was suggested or motivated by the prior art. The only motivation asserted by the examiner has to do with a supposed motivation to combine a use of computers with the method recited in claim 1. But that motivation, even if it existed, would be wholly insufficient to establish motivation or suggestion with respect to the underlying substance of the other features of the claim.

Thus, for example, it would not have been obvious to combine the various features of the applicant's claim 1, e.g., acquiring properties in exchange for interests in an investment entity, allocating each investor's basis among acquired properties, tracking the allocated bases as a result of exchanges of properties that fall outside of an investment profile for other properties in tax-advantaged exchanges, and determining current values of interests in the investment entity based on characteristics of the properties. (see claim 1; *see, e.g.*, OA, p. 6, the examiner said "it would have been obvious … to use a machine to carry out these steps, for the obvious advantage of efficiently carrying out the necessary functions," yet there is no assertion of a suggestion to combine the "necessary functions" in the first place.) *See Ecolochem, Inc. v. Southern California Edison Co.*, 227 F.2d 1361, 1372 (Fed. Cir. 2000) ("Although the suggestion to combine references may flow from the nature of the problem, defining the problem in terms of its solution reveals improper hindsight in the selection of the prior art relevant to obviousness." (internal cites and punctuation omitted)).

Using computers to do tasks in general that humans couldn't reasonably do manually may or may not be obvious, but identifying a particular task that no one had thought of before, possibly in part because it was not possible without a computer, would not have been obvious. That is the case here.

The examiner failed to demonstrate any actual suggestion to combine the various references other than his repeated statements that such combination was obvious or common knowledge. (*See, e.g.*, OA, p. 10, "In concluding that it would have been obvious …" Examiner referred to the obvious advantage of "efficiently carrying out the necessary functions;" p. 11,

"using computers to carry out operations in the field of finance is well known, and motivation to do so would have been found in the knowledge generally available.")

Broad statements that it was obvious to use computers are not the required identification of an actual suggestion to combine these various elements to produce the specific combinations claimed. If they were, then the requirement for a suggestion to combine would be rendered meaningless. The examiner also dismissed the applicant's reasoning that the fact that no one had previously combined the claimed elements despite the advantages of the combination supported non-obviousness, but made no attempt to actually rebut the applicant's argument, focusing on the mention of advantages rather than the point that there was no suggestion to combine the elements. (OA, p. 11)

Without an actual suggestion to combine the various elements, the examiner has failed to make out a proper prima facie case of obviousness. *See, e.g., In re Kotzab*, 217 F.3d 1365, 1371 (Fed. Cir. 2000).

Having failed even to assert the existence of certain features in any of the cited references, let alone the existence of any motivation or suggestion to combine the features of the claim, the examiner has not established that claim 1 would have been obvious.

Claim 16

Claim 16 was described by the examiner as "essentially parallel to claim 1" and then rejected on similar reasoning to what was articulated in the rejection of claim 1. (OA, p. 7)

Claim 16 is a system claim, while claim 1 is a method claim. Although the applicant does not dispute that there are similarities between the claims, the claims are different in ways that the examiner's short-hand "essentially parallel to claim 1" disregards.

Thus, although the examiner has failed to establish the obviousness of claim 1 for reasons similar to the ones stated above, there are additional reasons that make the examiner's position untenable.

1. Claim 16, unlike claim 1, refers to the investment entity specifically as one that is "for exchanging properties through tax-advantaged transactions." The examiner has not even asserted the existence of this feature in any of the cited references (including official notice).

2. Claim 16, unlike claim 1, recites that the investment profile comprises "a disciplined portfolio approach that uses diversification and contingent risk minimization." The examiner has not alleged the existence of this element in any of the cited prior art (including official notice).

3. Claim 16, unlike claim 1, recites a machine-based system to "(f) analyze other properties within the investment profile for possible investment by means of tax-advantaged transactions and to determine which properties held by the investment entity fall outside the investment profile and transactions and which are suitable for disposal." Nothing has been said by the examiner about this feature.

4. Claim 16, unlike claim 1, refers to enhancing properties by "refurbishment and management efficiencies." The examiner has failed to address this feature other than stating that similar language in claims 9 and 10 is "well known and obvious." (*see* OA, pp. 6-7)

5. Claim 16, unlike claim 1, refers to a "plan of redemption of interests of investors." Nowhere has the examiner even asserted the existence of this feature in any of the cited references (including official notice), except to say that "limitations on withdrawals or liquidations of investments are known and motivated" with regard to claim 29. (OA, p. 12)

6. As explained with respect to claim 1, the examiner also has not described any motivation or suggestion for combining pairs or all of the features of claim 16.

<u>Claim 29</u>

Claim 29 was described by the examiner as "essentially parallel to claim 1 with claim 8 included, and ... rejected on essentially the same grounds." (OA, p. 8)

As explained for claim 16, claim 29 has features that differ from claim 1. The examiner has failed to address those features in any way and has made no assertion that they are found in any of the cited references. Nor has the examiner explained how the combination of all of the

features of claim 29 would have been motivated or suggested. Thus, the examiner has failed to give an adequate rejection of claim 29.

For example:

1. In claim 29, unlike claim 1, the properties are acquired from the investors "at a succession of different times." This point was not addressed in any way by the examiner.

2. In claim 29, unlike claim 1, the properties that are identified as falling outside the investment profile are exchanged at "a succession of different times." The examiner has said nothing about this feature.

3. In claim 29, unlike claim 1, the interests of investors are redeemed at "a succession of different times." The examiner has given no citation for this feature in the prior art.

4. In claim 29, the rate of redemption of interests is controlled "to reduce the need to divest properties at depressed values" to fund the redemptions. The examiner implies that this feature is essentially the same as the feature of claim 8. (*see* OA, p. 12) This is incorrect, and the examiner has given no basis for the existence of this feature in any of the cited references.

<u>Claims 2 and 17</u>

Claims 2 and 17 recite that the investment profiles comprise investment-producing real estate. The examiner merely states without citation that it is common to invest in this type of real estate. (OA, p. 6) Regardless of what types of real estate it may be common to invest in, the cited references do not provide any motivation to combine or alter any of the limitations of claims 1 or 16, as explained above, and from which these claims depend. Thus, for the reasons discussed above with respect to claims 1 and 16, the cited references neither disclose nor would have made obvious the subject matter of claims 2 and 17.

<u>Claims 3 and 18</u>

Claims 3 and 18 recite that the investment profiles of claim 1 and 16, respectively, comprise inner-city residential properties. The office action rejected claim 3 together with claim 2 and claim 18 as parallel to claim 3. (OA, p. 6-7) For the reasons discussed with regard to

claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 3 and 18.

Claims 4 and 19

Claims 4 and 19 recite that the investment profiles of claim 1 and 16, respectively, comprise distressed properties. The office action rejected claim 4 together with claim 2 and claim 19 as parallel to claim 4 and rejected on the same grounds. (OA, p. 6-7) For the reasons discussed with regard to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 4 and 19.

Claims 5, 13, 15, and 20

Claims 5, 13, 15, and 20 recite that the investment profiles of claim 1, 2, 3, and 16, respectively, comprise properties for which the purchase price divided by the total rent obtained is low relative to other properties in the area. With regard to claim 5, the office action merely states without citation that it would be obvious that such properties may be good investments. The office action rejected claims 13, 15, and 20 as parallel to claim 5 and rejected on the same grounds. (OA, p. 6-7) For the reasons discussed with regard to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 5, 13, 15, and 20.

Claims 6, 12, 14, and 21

Claims 6, 12, 14, and 21 recite that the investment profiles of claims 1, 2, 3, and 16, respectively, comprise residential properties for which rents are below market for the proximate neighborhood. The office rejected claim 6 together with claim 5 and claims 12, 14, and 21 as parallel to claim 6 and rejected on the same grounds. (OA, p. 6-7) For the reasons discussed with regard to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 6, 12, 14, and 21.

Claims 7 and 22

Claim 7 recites that the investor of claim 1 makes a tax-advantaged contribution of property in exchange for an interest in the investment entity. Claim 22 similarly recites that the tax-advantaged contribution of claim 16 comprises a tax-advantaged contribution of property. With regard to claim 7, the office action merely states that Ward discloses this and that this was set forth with regard to claim 1. (OA, p. 7) The office action rejected claim 22 as essentially parallel to claim 7 and rejected for the same grounds. (OA, p. 7) Thus, for the reasons discussed above with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 7 and 22.

Claims 8 and 23

Claim 8 recites that the redemption of interests of investors of claim 1 is limited at any one time to a predetermined portion of a value of the properties held by the investment entity. Claim 23 similarly recites that the plan of redemption of claim 16 comprises such a limitation. With regard to claim 8, the office action merely states without citation that such limitations are well known, making the claim obvious. (OA, p. 7) The office action rejected claim 23 as essentially parallel to claim 8 and rejected for the same grounds. (OA, p. 7) Thus, for the reasons discussed above with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claims 8 and 23.

Claim 9

Claim 9 recites that the physical improvements of claim 1 comprise refurbishment. The office action merely states without citation that this is well known and obvious. (OA, p. 6) For the reasons discussed above with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 9.

Claim 10

Claim 10 recites that the property value in claim 1 is enhanced by improved management of the property. The office action merely states without citation that this is well known and obvious. (OA, p. 6) For the reasons discussed above with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 10.

Claim 11

Claim 11 recites that the investment profile of claim 2 comprises distressed properties. The office does not provide any reason for the rejection of claim 11. For the reasons discussed above with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 11.

Claim 24

Claim 24 recites that the management entity of claim 16 is the same as the investment entity. The office action states that Ward discloses this, referring to two particular sections. (OA, p. 7) The cited sections describe that in an LLC, the managers may be the owners, but do not refer to a "management entity." (*see* Ward, pp. 2, 4) Even if Ward can be said to disclose a management entity that is the same as an investment entity, for the reasons discussed with respect to claims 2 and 17, neither it nor the other cited references disclose or would have made obvious the subject matter of claim 24.

Claim 25

Claim 25 recites that the investment entity of claim 16 receives cash investments. The office action states that Ward discloses this, referring to one particular section, which does disclose that capital contributions to an LLC can include cash. (OA, p, 7; *see* Ward, p. 2) However, for the reasons discussed with respect to claims 2 and 17, neither Ward nor the other cited references disclose or would have made obvious the subject matter of claim 25.

Claim 26

Claim 26 recites that the values of interests in the investment entity of claim 1 that are exchanged for properties are based on the current value. The office action states, without citations, that it is well-known for the values of interests to be based on the current value, and that for the value to be unrelated to the current value would be the exception. (OA, p. 6) Even if such a valuation is well-known, for the reasons discussed with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 26.

Claim 27

Claim 27 recites that the redeeming of interests by investors in claim 1 occurs at times determined by the investors. The office action states, without citations, that this is well-known, giving the example of an investor selling shares of stock. (OA, p. 7) Even if such a limitation is well-known, for the reasons discussed with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 27.

Claim 28

Claim 28 recites that the investment entity of claim 1 is a limited liability company. The office action states only that Ward discloses limited liability companies and partnerships. (OA, p. 7) The examiner does not explain how the existence of limited liability companies would make it obvious to use one as the investment entity of claim 1, not does he identify any other reference that does so. Even if such an arrangement were obvious, for the reasons discussed with respect to claims 2 and 17, the cited references neither disclose nor would have made obvious the subject matter of claim 28.

Conclusion

The examiner has failed to establish a prima facie case of obviousness, has reconstructed the claims in hindsight from features said to be found in two main references and a large number of additional materials, and has not even asserted the presence of at least some of the features of the claims in any of the cited references.

The applicant asks the Board to reverse the examiner and allow the claims.

Enclosed is a $500.00 check for the Appeal Brief fee and a $1,590.00 check for the Petition for Extension of Time fee. Please apply any other charges or credits to deposit account 06-1050.

Respectfully submitted,

Date: 1/6/6

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Appendix A—Claims

1. A machine-based method comprising:

acquiring one or more properties from one or more investors through tax advantaged transactions, at least one of the properties being acquired from one of the investors in exchange for an interest in an investment entity;

using a machine to (a) track each investor's basis in his interest in the investment entity, (b) allocate each investor's basis in his interest in the investment entity among properties acquired by the investment entity, (c) track the allocated basis of each investor as a result of a succession of tax-advantaged exchange transactions, (d) from time to time determine a current value of an interest in the investment entity based on characteristics of the one or more properties held by the investment entity, and (e) identify at least one of the properties as appropriate for disposition,

exchanging at least one of the identified properties that falls outside of an investment profile for at least one other property in a tax-advantaged exchange;

enhancing the value of at least one of the properties by physical improvements; and

redeeming an interest of at least one of the investors by the investment entity at a value based on the current value.

2. The method of claim 1 in which the investment profile comprises income-producing real estate.

3. The method of claim 1 in which the investment profile comprises inner-city residential rental properties.

4. The method of claim 1 in which the investment profile comprises distressed properties.

5. The method of claim 1 in which the investment profile comprises properties for which a purchase price for an individual property divided by a total rent obtained from such property is low relative to other properties located in a surrounding area.

6. The method of claim 1 in which the investment profile comprises residential rental properties for which rents are below market for a neighborhood proximate to such properties.

7. The method of claim 1 in which the investor makes a tax- advantaged contribution of the property in exchange for an interest in the investment entity.

8. The method of claim 1 in which the redemption of interests of investors is limited at any one time to a predetermined portion of a value of the properties held by the investment entity.

9. The method of claim 1 in which the physical improvements further comprise refurbishment.

10. The method of claim 1 in which the property value is further enhanced by improved management of the property.

11. The method of claim 2 in which the investment profile further comprises distressed properties.

12. The method of claim 2 in which the investment profile further comprises residential rental properties for which rents are below market for a neighborhood proximate to such properties.

13. The method of claim 2 in which the investment profile further comprises properties for which a purchase price for an individual property divided by a total rent obtained from such property is low relative to other properties located in a surrounding area.

14. The method of claim 3 in which the investment profile further comprises residential rental properties for which rents are below market for a neighborhood proximate to such properties.

15. The method of claim 3 in which the investment profile further comprises properties for which a purchase price for an individual property divided by a total rent obtained from such property is low relative to other properties located in a surrounding area.

16. A machine-based system of managing investment assets comprising

an investment entity for receiving tax-advantaged contributions of at least one property from at least one investor in exchange for an interest in the investment entity, and for managing, holding and exchanging properties through tax-advantaged transactions;

an investment profile comprising a disciplined portfolio approach that uses diversification and contingent risk minimization,

a machine-based system to (a) track each investor's basis in his interest in the investment entity, (b) record and analyze investments held by the investment entity, (c) allocate the basis and tax attributes of investments held by the entity among the investors, (d) track the basis and tax attributes allocable to each investor in the investments of the entity, (e) from time to time determine a current value of an interest in the investment entity based on characteristics of the one or more properties held by the investment entity, and (f) analyze other properties within the investment profile for possible investment by means of tax-advantaged transactions and to determine which properties held by the investment entity fall outside the investment profile and transactions and which are suitable for disposal;

at least one management entity to actively enhance properties held by the investment entity by means of physical improvements, refurbishment and management efficiencies; and

a plan of redemption of interests of investors, the redemptions occurring at a value based on characteristics of one or more of the properties.

17. The system of claim 16 in which the investment profile comprises income-producing real estate.

18. The system of claim 16 in which the investment profile comprises inner-city residential properties.

19. The system of claim 16 in which the investment profile comprises distressed properties.

20. The system of claim 16 in which the investment profile comprises properties for which a purchase price for an individual property divided by a total rent obtained from such a property is low relative to other properties located in a surrounding area.

21. The system of claim 16 in which the investment profile comprises residential rental properties for which rents are below market for a neighborhood proximate to such properties.

22. The system of claim 16 in which the tax-advantaged contribution comprises a tax-advantaged contribution of property.

23. The system of claim 16 in which the plan of redemption further comprises a limitation to a predetermined portion of a value of the properties held by the investment entity.

24. The system of claim 16 in which the at least one management entity is the same as the investment entity.

25. The system of claim 16 in which the investment entity also receives cash investments.

26. The method of claim 1 in which the values of interests in the investment entity that are exchanged for properties of investors through tax-advantaged transactions are based on the current value.

27. The method of claim 1 in which the redeeming of interests by investors occurs at times determined at least in part by the investors.

28. The method of claim 1 in which the investment entity comprises a limited partnership or a limited liability company.

29. A machine-based method comprising:

acquiring properties at a succession of different times from investors in tax-advantaged transactions in exchange for interests in an investment entity;

defining an investment profile for properties to be held by the investment entity;

identifying at least one of the properties as falling outside the investment profile and exchanging the properties in tax-advantaged exchanges at a succession of different times;

enhancing the values of at least some of the properties by physical improvements;

redeeming the interests of at least some of the investors at a succession of different times;

controlling the rate of redemptions of interests to reduce the need to divest properties at depressed values to fund the times;

each of the acquisitions and each of the redemptions being effected at the then current value of the interests of the investors based on the characteristics of properties held by the investment entity; and

using a machine to (a) track each investor's basis in his interest in the investment entity from his initial investment to a redemption of his interest, (b) allocate each investor's basis in his interest in the investment entity among properties acquired and held by the investment entity, and (c) track the allocated basis of each investor's interest as a result of a succession of tax-advantaged exchange transactions involving properties acquired, held, and divested by the investment entity at a succession of different times.

Appendix B—Evidence relied upon by the examiner

The examiner relied upon the following references (copies attached).

B1 Anonymous, "ASA Knocks Instant Access," Bank Marketing International, n. 90, p. 5, Mar. 1996.

B2 Anonymous, "Halifax Account Wrangle," Financial Times, p. IV, Dec. 7, 1991. [Only the abstract was provided, but this was not indicated in the examiner's citation.]

B3 Anonymous, "PUTNAM COS: Putnam's New Average Cost Basis Statement to Make Shareholder Job Easier at Tax Time," Business Wire, Apr. 2, 1991.

B4 Anonymous, "Technology Review," Pension World, v. 29, n. 9, p. 37, Sept. 1993.

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2088132 Supplier Number: 02088132 (THIS IS THE FULLTEXT)

ASA knocks instant access

(Complaint against Direct Line Financial Services's use of words 'instant access' could bar all bankers from using the term in all advertising and marketing)

Bank Marketing International, n 90, p 5
March 1998
WORD COUNT: 504

TEXT:
A ruling this month by the Advertising Standards Association could affect the entire retail banking industry in the UK. Scott Anderson reports

IN A move which could have a knock-on effect for the entire retail banking industry, the UK's Advertising Standards Authority (ASA) has upheld a complaint against Direct Line Financial Services following a year long investigation into the words 'instant access'.

Analysts said the judgment could outlaw the use of the term in all advertising and marketing and has implications for all bankers.
The complaint centred round objections to an advertisement that was headlined "Direct Line Instant Access Account". The complaint objected that, to withdraw money, customers had to telephone Direct Line to have the money transferred to an existing bank or building society (which took three working days).

The customer would then be bound by that institution's procedures before they had access to the funds. Therefore, they objected to the description of the account as 'instant access'.

The ASA upheld the complaint commenting that consumers would expect immediate access to their money and have asked Direct Line to remove it from all advertising and to include a qualifying statement.

Direct Line Financial Services' managing director Stephen Geraghty said: "This ruling has the potential to cause more confusion than it resolves. As the ASA themselves acknowledge, many companies describe their accounts as instant access in similar circumstances to those which have led to the ruling against Direct Line.

"Until recently, instant access was always used to mean that customers could get at their **money** without giving notice or paying a penalty. This ruling means that accounts where cheques must be issued or payments made through banking systems cannot be advertised as offering instant access. This rules out postal accounts or accounts where only a **limited amount** of cash can be **withdrawn** at a time."

In the judgment, ASA said that Direct Line claimed in its defence that they thought the account fell within the definition of an instant access account as laid down by the Bank of England.

A spokesman for the Bank of England, however, said that it has no such definition and did not know what Direct Line had referred to.

Direct Line also said they believed that they were complying with the British Bankers' Association (BBA) Code of Conduct, which issues guidelines on advertising.

BBA assistant director Brian Morris said "the specific circumstances of their case are not dealt with in our code and, to that extent, they have complied with it. We recognise that our code is in need of review, not just in this area but in others, as it has not been updated since 1990."

As ASA judgments are not binding on other institutions, it is not clear at

this stage what the full implications of the judgment are but, in practice, the ASA is likely to take a similar line with others.

The Building Societies Association also said it is conducting an industry review into their code of conduct for the advertising of interest bearing accounts.

04686544
Halifax account wrangle
UK - HALIFAX'S INSTANT XTRA ACCOUNT PROFILED
Financial Times (C) 1991 (FT) 7 December 1991 pIV

Halifax Building Society (UK): this Finance & the Family article reports on the Halifax Instant Xtra account. A depositor opened a joint account in August (1991) on the understanding that he would have immediate access to the **money** , as described in the Halifax's promotional leaflet. He was shocked to receive a letter from head office several months later to infirm him that the society had imposed 28 days notice of withdrawal on his account. The Halifax referred him to a copy of the society's rules which state: "the Board may at any time and from time to time and without any notice **limit** the **amount** that may be **withdrawn** from the Society in any month by the investing members." The depositer had never heard of this rule, and it would be surprising if he had, since it is tucked away in a document which is only available on request. The Instant Xtra Plus account is a high interest accoun t, which currently pays out 10.7 per cent gross on balances of over GBP 50,000. The depositor had moved sums of just under GBP90,000 three times in the four months of the account and believes this to be the reason that the 28 day notice was put on to the account. Halifax has invoked the rule fewer than 10 times this year. "Building societies have radically changed their operations to compete more directly against banks but Halifax's response would suggest that it regards itself more as a savings institution than a bank", said the depositor. (Abstract)**

0219846 BW602

PUTNAM COS: Putnam's new average cost basis statement to make shareholder job easier at tax time

April 2, 1991

Byline: Business Editors

FEATURE...

BOSTON--(BUSINESS WIRE-FEATURES)--Putnam solves its shareholders' cost basis problems with the new "Average Cost Basis Statement"--among the industry's first -- that computes, for tax purposes, the gain or loss on Putnam fund shares redeemed during 1990.

"Average cost basis is one of four new or improved services we offer shareholders at tax time in our continuing effort to be the best service provider in the mutual fund industry," said Robert Lucey, President of Putnam Investor Services.

Shareholders must establish a cost basis to calculate the amount of capital gain or loss on the redeemed shares when completing their tax returns.

Lucey pointed out that **investors** who do not keep **track** of the cost **basis** of their **mutual fund** shares run the risk of paying taxes twice on the same principal -- once when it is earned or reinvested in additional shares and again when they redeem shares.

The difficulty comes, said Lucey, when a shareholder begins adding shares to an account. Almost inevitably, the cost of the newly acquired shares will be different from those acquired at other times. For shareholders who reinvest distributions, this occurs each time the fund makes a distribution.

Although shareholders do not receive a check for distributions reinvested in fund shares, the IRS considers it income generated in the year the distribution is declared, and shareholders are liable for income taxes to the same extent as if it were paid in cash. If the shareholder does not take this into account when redeemeing shares, taxes may be paid again on the portion of the proceeds representing the reinvested distributions.

To avoid this double taxation on shares, investors must add the cost of newly acquired shares to the cost of shares already held. The new statement will provide average cost basis only on accounts opened in 1985 or after. The new service will begin with the February statement.

Average cost is one of four ways to calculate cost basis. Under certain circumstances, one of the other three may be preferable -- "first in, first out" where the first shares purchased are the first shares redeemed; redemption of a specific block of shares, providing the shareholder has kept careful records and can properly indentify shares; or separating shares, a complicated process that distinguishes between shares held long term (a year or more) and short term (less than a year) and calculate the average cost for each category.

Shareholders are urged to consult their tax advisors or see IRS Publication 564, "Mutual Fund Distributions."

Putnam also announced three other new or improved services that make tax time easier. They are:

o a consolidated Form 1099 that provides in a single package information on all shareholder's 1990 distributions and redemptions;

o a special "Tax Savings Report" for shareholders of Putnam's tax-exempt funds that provides similar consolidation; and

o a new transcript policy. Trancripts for the two years immediately preceding the current calendar year may be obtained at no cost. A $10 fee is charged for each request for transcripts covering earliers years, regardless of how many years are specified in the

request.

Putnam is one of the largest and oldest investment management firms in the country with more than $42 billion in assets under management for mutual fund shareholders and pension funds.

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Technology review

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ABSTRACT: Five software packages and systems are reviewed: 1. Merrin Financial Trading Platform, by Merrin Financial Inc., 2. AIM 4.41, by Wyatt Software, 3. AlexStat, by Alexander & Alexander Consulting Group, 4. CompuVest Tax Tracker, by Jones & Babson, and 5. FDP/DAILY, by Financial Data Planning Corp.

TEXT: Merrin Financial Trading Platform (computerized trading system, $2,500/mo. or $30,000/yr.) Merrin Financial Inc., 1250 Broadway, New York, NY 10001, (212) 563-3700.

Merrin Financial's trading system has evolved into a "platform" that is being used as an industry-standard gateway to inexpensively and efficiently connect money managers to a growing number of on-line research, quote, news, brokerage, execution, clearing and custodial systems. Assessing and integrating many services in this manner increases the level of efficiency with which money managers and brokers can work, thereby promoting the growth of seamless electronic connections throughout the securities industry. The result is increased volume and performance at lower per unit costs.
The Merrin Platform can manage, integrate and disseminate trading information from more than three dozen internal and external portfolio management/accounting systems; clearing/service bureaus and custodian banks; quote services with on-line pricing feeds; and, a growing number of execution/list/matching systems. The Merrin Platform can be used for institutional money management and brokerage, OTC market makers, fixed income, and global trading--and can be enhanced with the real-time CompALERT compliance system. It runs on off-the-shelf IBM compatible PCs and Novell networks under the DOS operating system.

AIM 4.41 (enhancement to AIM system, contact vendor for pricing information) Wyatt Software, 5335 S.W. Meadows Road, Suite 200, Lake Oswego, OR 97035, (503) 598-4472.

AIM 4.41 is an enhancement to Wyatt's AIM system, which enables investment managers to comply with new performance reporting standards adopted by the Association of Investment Management and Research (AIMR). The standards require that investment managers report time-weighted rates of return for composite portfolios that include all active accounts. The composite should be dollar-weighted, based on beginning of period balances.

AIM 4.41 enables managers to import and store portfolio balances and cash

flows, compute individual portfolio time-weighted rates of return, and use the system to create composites based on the market values (balances) of the return files.

AlexStat (data analysis service, call vendor for pricing structure) Alexander & Alexander Consulting Group (A&ACG), 125 Chubb Ave., Lyndhurst, NJ 07071, (201) 460-6644.

AlexStat is a new generation of computerized health care data analysis service to help employers strategically manage their benefit programs. The service uses claims as well as other data maintained by managed care plans, employer coalitions, and state and federal governments, to produce information for health cost and quality management.

The service performs five major types of analysis: (1) plan financial performance (2) inpatient cost and utilization (3) ambulatory cost and utilization by type of service (4) lifestyle-related and catastrophic illness by diagnosis, to provide information for health promotion and utilization management; and (5) health care quality and outcomes management information for use in selecting managed care vendors and providers.

AlexStat is commonly used to diagnose excessive health care costs and utilization in health plan experience. The system can also project the cost of employer liabilities for post-employment and retirement benefits under FAS 112 and FAS 106.

CompuVest Tax Tracker (software, $29.95, disk that includes three applications) Jones & Babson, Three Crown Center, 2440 Pershing Road, Kansas City, MO 64108, (816) 471-5200.

CompuVest Tax **Tracker** is a new, easy-to-use PC program that helps investors calculate taxes on their **mutual fund investments** and provides the cost **basis** for each redemption, or sale, of shares and helps an investor determine the most favorable tax treatment to use when filing taxes. The disk illustrates which of the three tax basis calculation methods accepted by the IRS is most favorable for the individual's situation.

The Tax Tracker is the newest investment program offered as part of Jones & Babson's unique CompuVest disk program, but there are other useful programs on the new disk as well. The Investment Tracker keeps a record of all of an investor's mutual fund transactions on a PC. It stores fund data, calculates market value and even shows what percentage of an individual's investments are in a particular fund.
A third application on the new CompuVest disk is the Investment Planning Calculator, which lets the investor find answers to key questions, such as how much is needed to invest to achieve a specific amount in the future.

FDP/DAILY (software system) and FDP/a4 (software) (contact vendor for pricing structure; flat fee for product plus monthly maintenance charge for support and legislative updates) Financial Data Planning Corp., 2140 South Dixie Hwy., Miami, FL 33133, (305) 858-8200.

FDP/DAILY is an "on-demand" participant record keeping and plan administration software system for defined contribution plans. Administration functions on FDP/DAILY are reduced to tasks that can be performed on an "as needed" basis. The system design allows you to offer variable frequency processing for your plans within one system environment. It offers a generic data import feature that accommodates links to most investment houses or brokerage firms.

FDP/DAILY is designed to expedite processing, offering the ability to collect, process and report information on a timely basis.

FDP/a4, has been designed to perform nondiscrimination testing under the 401(a)(4) and 410(b) regulations. It is an open system for PCs, allowing the user to import and test data from any valuation/record-keeping system

through an ASCII file import capability. In addition to performing the Ratio Percentage Test and the Average Benefit Test, FDP/a4 helps create plan designs that fall outside of the regulatory safe harbors using the general nondiscrimination test. The software performs rate group restructuring, considers family aggregation and allows illustration of cross-tested "new comparability" designs.

THIS IS THE FULL-TEXT.

DIALOG(R)File 148:Gale Group Trade & Industry DB

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Taking care of no. 1: financial planning.(Continuing Education)
Basara, T. Scott; Basara, Lisa Ruby
Drug Topics, v139, n9, p68(10)
May 8, 1995

TEXT:

Introduction

To most people, financial planning is what happens after taxes and bills are paid and money is left over. Placing this money in savings accounts, certificates of deposit (CDs), or whatever investment is most convenient, and then hoping for a reasonable interest rate of return, is often the only "planning" that is done.

In actuality, financial planning is the process by which individuals evaluate their current and potential financial situation and systematically design an investment strategy to achieve desired financial goals. While this process does involve time and insight into various investment options, most professionals with access to relevant financial literature and other resources can he very effective at managing their money, investing successfully, and planning for a comfortable retirement.

This article will provide the pharmacist with information regarding various aspects of the financial planning process and will discuss various investment options, including their advantages, disadvantages, risks, and benefits. While an introduction to financial planning of this sort is not intended to replace the advice of a financial planner or an accountant, it can improve your knowledge of and ability to select wise investment options.

Who should plan?

All individuals should plan their finances to some degree, regardless of their career or life stages. The degree to which you plan depends on your financial goals. Assuming that your income is high enough to cover your living expenses and that you have discretionary monies remaining at the end of each month to spend in some way, what do you want that money to do? Allow you to take a vacation? Earn interest for your child's college tuition? Secure your future in a retirement account?

Each of these goals requires a different investment strategy. A review of your net worth will help you determine how much you can afford to invest without adversely affecting your lifestyle. And your decision on your financial objectives will influence your investment strategy selection. No matter what your goals or financial position, you will benefit from logical financial planning.

When should you plan?

As soon as you have discretionary income (you are earning more than enough money to pay living expenses), financial planning is appropriate. Although it is fun, reckless spending of discretionary income on consumer goods and luxuries is not advisable if winning the state lottery is not in your future. Most people must consider the long-term needs of their spouses, their children, and themselves (i.e., retirement) as they progress through life. The sooner you think about these needs, the more likely you are to meet them successfully in the always unknown and sometimes risky future.

How should you plan?

There are five steps to financial planning:

* First, you must set your goals and ascertain your discretionary income.
* Then, within your goals and your income, you must select the most appropriate investment alternative(s).
* After making investment choices, you must allocate your money among these alternatives.
* Then, you need to monitor and analyze the performance of your investments.
* Finally, you should review your investments regularly to ensure that as your goals change, your investments are still appropriate and that they are performing optimally.

These five steps of financial planning will help ensure that your **investment** are wise and productive.

Setting goals, assessing income

How much **money** can you invest? The amount of **money** you can afford to invest depends upon your net worth. To ascertain your net worth, consider and quantify the components of net worth that are listed in Table 1.

A review of your monthly budget will help in quantifying many of these items. Several computer software packages are available to facilitate home budgeting, investing, and assessment of personal finances. Quicken (a product of Intuit of Menlo Park, Calif,) is just one example of an inexpensive software program ($50 to $70) that allows computerized bookkeeping, including categorization of expenses, monthly budgeting, **investment** monitoring, and assessment and reporting of your financial position.

You can quantify your monthly expenses even if you do not have a computerized software package. The best way to begin is by creating a worksheet that categorizes all of your expenses. Document all spending for a given time period--perhaps two months. Identify expenses that you consider necessary and expenses that are potentially unnecessary. Table 2 identifies several **money** -saving ideas to consider.

As that old saying goes, "In one hand and out the other." When people live beyond their means, saving **money** is difficult. However, by cutting back a little in the short term, you can save in the long run. For example, assume you have a newborn child, and you can begin saving just $25 per week to help pay for his college education, which begins at age 18. Figure 1 illustrates how quickly saving just $25 per week can add up over this time. As you can see, if you invest $25 a week at an annual return of 8%, you will accumulate $52,260 in 18 years. The power of compounding interest on your weekly **investment** makes these results look dramatic.

Once you know how much **money** you have available for investing, you need to consider how much risk you are willing to accept. Risk and rewards are directly related in investing: The more risk you accept, the greater the potential return. However, equally great is the potential for loss. Also, more conservative **investments** generally have lower rates of return.

Risk is a multifaceted concept and includes interest rate risk, liquidity risk, market risk, taxation risk, and inflationary risk. When you select a particular **investment** option, such as stocks, savings bonds, or retirement accounts, your **money** may be easy or difficult to access. This is known as liquidity risk. Because stocks can be traded relatively easily, they are considered very liquid **investments** .

Savings accounts can also be accessed quickly to provide cash. However, savings bonds and CDs must be held for a specified amount of time before they can be cashed in at full projected value. **Money** invested in individual retirement accounts (IRAs) cannot be accessed without a penalty until the investor reaches age 59 1/2 (except for hardship, etc.). Clearly, if your goals are to save **money** for a purchase in the near future, such as a new house or a child's tuition, a relatively liquid **investment** strategy is appropriate.

Interest rates, tax rates, tax laws, the economic market, and the rate of inflation are all relatively uncontrollable factors that make various **investment** options more or less attractive at any given time. For example, in early to mid-1994, interest rates on mortagages were quite low, making real estate and home buying attractive. In 1995, mortgage rates have increased in response to the Federal Reserve Board's interest rate increases, and home buying is no longer as feasible for many individuals. At the same time, the federal government is taking steps to make IRAs more appealing by loosening tax restrictions and permitting early withdrawal of **funds** for specific purposes, such as purchasing a new house.

Investments options

Regardless of your financial goals (i.e., vacation, car, education, retirement), the following information about different types of **investment** options is relevant. When choosing among **investment** options, keep in mind how much risk you are willing to accept and the amount of your discretionary income.

Savings accounts: Savings accounts can be opened at various financial institutions, including banks, savings and Ioans, and credit unions.

Savings accounts are the most liquid short-term **investments** and are great places to invest emergency cash. Be sure to select a solid financial institution that federally insures your savings balance.

Money market accounts: **Money** market accounts are similar to savings accounts. However, **money** market accounts usually have a minimum-balance requirement and sometimes **limit** the **amount** and number of **withdrawals** permitted in a given time period. As a consequence, **money** market accounts generally pay higher interest rates than savings accounts do.

Treasury bills: Treasury bills are issued by the U.S. Department of the Treasury and typically mature in either three or six months. Treasury bills are issued in denominations of $10,000 or more, making them appropriate for investors with large amounts of discretionary income.

Savings bonds: Through the Federal Reserve, the United States Treasury offers two types of savings bonds: Series EE and Series HH. Savings bonds are sold direct from the Treasury or through financial institutions (i.e., savings and loans, commercial banks) that qualify as savings bonds agents. Series EE bonds are sold at half their face value in denominations ranging from $50 to $10,000. They are an appreciation-type security, earning interest until their maximum maturity--usually 30 years.

Series HH bonds are issued in denominations of $500, $1,000, $5,000, and $10,000. However, Series HH bonds issued on or after March 1, 1993, earn interest at an annual rate of 4%. As you can see, the lower risk associated with savings bonds is matched by lower interest rates.

One advantage of savings bonds is a tax break associated with their use in payment of education expenses. Interest earned on Series EE bonds purchased after Jan. 1, 1990, can qualify for exclusions from federal income tax if the bond owner paid tuition to a college, university, or a qualified technical school during the year in which the bonds were cashed.

Stocks: Shares of stock represent ownership in a corporation. But because the value of a stock can decline and because there is no guarantee that a corporation will pay dividends to its shareholders, stocks are a much riskier investment. Although publicly traded stocks report to the Securities & Exchange Commission (SEC), they are not federally insured.

However, the value of stocks also can appreciate, and many companies do disburse dividends. Therefore, stock ownership can be very profitable. The average rate of return earned for specific stock investments as published in a 1993 study was between 9.6% and 12.6%. In particular, pharmaceutical industry stocks have performed quite well in the past year and remain key holdings for many investors.

When selecting companies in which to invest, you should consult the security's prospectus for any public company making an initial public offering. A prospectus must fully and fairly disclose sufficient information about a company's financial history and its management to permit investors to judge the merits of investment. Other financial information that you can obtain for publicly held companies includes both a quarterly and an annual report that have been filed with the SEC. Additionally, public libraries often have access to on-line services that provide detailed summaries of performance histories, current financial conditions, and future prospects of publicly held companies. These information services evaluate both the risk and the timeliness of an investment in each company's stock.

Brokerage houses also provide such information, but for a fee. Full-service brokerage houses have research departments that continually compile and update financial information that can be requested by clients of the firm.

If you are interested in purchasing stocks, you must open an account at a brokerage firm, such as PaineWebber, Merrill Lynch, or Smith Barney. When selecting a broker, remember that brokers usually make money with every transaction. Be sure that your broker explains what fees will be charged for your investment.

Be wary of consultants who suggest transfers from one investment to another without reasonable justification; they may simply be improving their commissions rather than your financial position. According to a recent study, not all brokerage firms pay special attention to their investors. Many brokers will explain that there is a risk that you could lose money with a stock purchase, but they fail to fully explain the

possible losses with other investments. Table 3 provides a list of questions to ask your financial advisor to help you understand more about your investment.

Mutual funds: A mutual fund pools the monies of many people, investing them in stocks, bonds, money market accounts, and other securities. In theory, mutual fund owners rely on the expertise of a fund's investment manager or managers, who are responsible for the fund's performance. In many cases, money placed in a fund will be diversified among various types of investments, such as industrial, retail, and transportation, with the belief that the risk of loss in one industry will not carry over to another industry.

As an example, consider the diversification achieved by the management of Vanguard's High Yield Corporate Bond Fund on July 31, 1993. The fund held, at that time, investments in 15 different industries, among them consumer goods, grocery stores, media and communications, retail stores, and food and lodging. This type of diversification helps guard against losses that may occur if hard times fall on one particular industry. Although many investors allocate their money in different types of investments (i.e., stocks, bonds), most people do not have enough cash knowledge or insight to diversify successfully among different industries.

Additionally, you can diversify your mutual fund investment by selecting different types of mutual funds, such as equity funds or corporate bond funds.

Table 4 further demonstrates the extent of diversification that can be achieved in a mutual fund. Note the various companies within the different industry segments. As you can see from the sample of portfolio holdings in the Vanguard Group's High Yield Corporate Bond Fund, an investor's money is diversified by industry type as well as by company within each industry. Mutual funds also provide an excellent investment vehicle for investors who would not otherwise have the opportunity to purchase various stocks and bonds and yet retain immediate access to their investments.

All mutual funds have stated objectives, minimum investment amounts, and risk profiles. Before investing in a mutual fund, obtain the fund's prospectus and the latest annual report that provides detailed information about the fund. Unlike stocks, where a prospectus is created for an initial public offering, mutual funds periodically prepare a prospectus for investors. The following is a list of items that are usually found in a mutual fund prospectus:

* Information about opening an account
* Financial highlights
* Investment objectives
* Investment policies
* Types of investment risks
* Investment limitations
* Information about the portfolio's share price
* Shareholder's guide: information about purchasing, selling, and exchanging shares and other miscellaneous management policies

When you invest in mutual funds, shares are purchased from an investment group, such as Vanguard or Dreyfus, at a price that is recalculated every business day. Often these shares can be purchased through the mail (i.e., sending a check to the investment group). Once an account is opened, most brokers will allow you to authorize them to automatically deduct a set amount from your checking account. Again, this is a convenient way to put money aside before you have the chance to spend it. Remember, however, that although they are regulated by the SEC, mutual funds are not federally insured, which makes them slightly more risky. As a result, they generally earn a higher rate of return compared with a savings account.

If you are considering investing in a mutual fund, there are several useful information sources, such as financial magazines and investment consultants. For example, mutual funds are ranked in periodicals such as Forbes, Money, and U.S. News & World Report. Rates of return, performance histories, investment strategies, minimum investment requirements, and management fees are key characteristics that should be compared among funds.

Information summary

There are many resources available to help you determine where to make your investments. Table 5 provides suggestions about where you can start if you want more information.

Investing for retirement

While these investment alternatives can be used to save money for retirement, there are other options that can prove more profitable for long-term financial needs.

As government budget cuts and reforms loom on the horizon and the baby-boom generation ages, the Social Security program has become vulnerable. For most people, Social Security alone is unlikely to provide sufficient retirement income. Current planning through individual retirement accounts, as well as employer-sponsored and self-employed retirement plans, will help prepare for a financially secure retirement. This section describes various retirement options, including their risk profiles, liquidity characteristics, and tax advantages and disadvantages.

Individual retirement accounts

Money placed in an individual retirement account (IRA) can be invested in stocks, bonds, mutual funds, savings accounts, and real estate. One can think of IRAs as umbrella accounts that cover many types of investments, thereby giving the investor many options. While anyone can contribute to an IRA, only certain people can take advantage of the tax breaks associated with IRAs. If you are not currently covered by a pension, profit-sharing, or other tax-advantage retirement plan, the following criteria must be met for your contribution to be fully or partially deductible on your tax return: taxpayer. Because you were already taxed on a nondeductible contribution, you are required to report this contribution to the Internal Revenue Service using Form 8606. This will prevent you from having to pay a double tax on this contribution when the money is withdrawn from the plan after age 59 1/2.

Table 6 illustrates the value of tax-deferred investing. If you invest $2,000 per year in an IRA at a 10% interest rate for 30 years, you can earn $133,131 more than if you choose not to contribute to an IRA.

Figure 2 illustrates the difference in the rate of return over a 30-year period for the above $2,000-per-year investment at 10% on both a tax-deferred investment and a nontax-deferred investment.

Because the tax-deferred investment is not paying taxes on the interest, it will grow at a quicker pace as the investment balance increases. As you can see in Figure 2, the tax-deferred investment grows much quicker as the investment balance increases. Another benefit of IRAs is your lower tax rate: If you withdraw your tax-deferred investment when you retire, your overall income is often lower, and you pay taxes at a lower rate. The full benefits of an IRA (a qualifying tax-free contribution; deferral of tax on related interest, dividends, and gains; and withdrawal at lower tax rates) make IRAs a viable and worthwhile way to save for retirement.

Disadvantages of IRA contributions

Although there are many advantages to contributing to an IRA, there are some drawbacks. One of the major disadvantages of contributing to an IRA is the long-term nature of the investment. If you withdraw from an IRA prior to age 59 1/2, a penalty of 10% of the withdrawal, in addition to the requirement to pay tax on the withdrawn amount, is assessed.

To ensure that your nondeductible IRA contribution, which is limited to the lesser of $2,000 per year or 100% of your compensation, is not taxed again when the money is withdrawn at retirement, Form 8606 must be maintained and carried forward from year to year until retirement.

Other retirement options

If you are not making a contribution to an IRA, it is probably that you do not qualify for a deduction because you are covered by an employer-sponsored retirement plan. With today's unstable work environment and economy, many jobs are not secure. In this case, your retirement benefits may include those accumulated from several jobs. Therefore, the financial success of your retirement will depend on how well you record and manage your employer-sponsored plans. This section highlights retirement plans that allow you to make contributions as well as plans in which contributions are made by your employer.

401(k) plans: Large pharmacy chains might offer employees the opportunity to participate in a 401(k) retirement plan, which is a

tax-deferred savings plan. Like a mutual fund, a 401(k) invests in various types of securities, bonds, and cash equivalents. Contributions that are deducted from your salary before taxes are limited to a specific amount (20% of wages--up to a total amount of $9,240--was the maximum amount allowed in 1994). All or part of this deduction may be matched by your employer. Most 401(k) plans require that employees become vested (i.e., work for a predetermined number of months or years) prior to earning the right to accrued employer contributions.

Because of employer matching, 401(k) plans can be very profitable for participants. For example, Mary, a pharmacist, works for Joe's Pharmacy and earns $50,000 per year. Joe's Pharmacy established a 401(k) plan and will contribute 50 cents for every dollar that Mary contributes, up to 4% of her income. If Mary contributes 10% of her income to the 401(k) in 1994, the total 401(k) contribution is calculated as follows:

As with an IRA, contributions to 401(k) plans are penalized if withdrawn prior to age 59 1/2. However, additional taxes are not assessed for distributions that are:

* Made to a beneficiary or to the estate of the participant on or after his or her death
* Made because the participant is totally and permanently disabled
* Paid to another person designated in a qualified domestic relations order
* Paid to the employee to the extent that the employee has deductible expenses for medical care (whether or not the employee itemizes deductions for the tax year)
* Money can be borrowed from the 401(k) plan without penalty. Interest on the loan is paid back to the plan, rather than a bank, and is not tax-deductible. When starting a 401(k) plan, review the investment options offered and, whenever possible, minimize risk by dividing your 401(k) contributions among two or more types of investments, such as conservative long-term mutual funds and riskier short-term stocks. In this way, the likelihood of earning an adequate return rate is maximized.

Pension plans

Some corporations still provide pension plans for employees. Most pension plans provide for periodic payments after retirement for the rest of the employee's life.

The amount of money received from an employer is defined in the pension plan and is usually determined on the basis of the employee's average salary as well as the number of years that the employee has worked for his or her company. Because the pension plan is funded by your employer, and the process by which benefits are calculated is predetermined, you simply need to understand how the pension plan is designed in order to calculate the amount of money you can expect upon retirement.

Note that if you work a few more years at, presumably, a higher salary, your monthly pension benefit can become substantially higher. If the above calculation is modified to reflect an additional three years of work which would increase the average salary, the difference for the monthly pension benefit amount can be seen as follows:

You can see that an additional three years has increased the monthly pension benefit by $465 per month. When you are considering retirement, it is important to pay attention to the characteristics of your pension fund to maximize its payout.

Planning retirement for the self-employed

For self-employed pharmacists, a Keogh plan or an IRA simplified employee pension plan can be an ideal way to cut taxes and contribute to a retirement plan for you and your employees. Because of the complicated rules and different objectives of these plans, it is recommended that you consult your accountant or financial planner to determine your best alternatives.

Keogh plans: If you are self-employed, and you have earned income from your business, you can set up a retirement plan known as a Keogh plan. A Keogh plan may be either a defined-benefits plan or a defined-contribution plan.

A defined-benefits plan promises a fixed benefit at retirement, and contributions are determined using actuarial data. In a defined-contribution plan, contributions are typically made on the basis of

a percentage of earnings and can vary from year to year. Some of the rules governing Keogh plans are as follows:

* Keogh plans must be established before the end of the tax year.
* The plan must be written.
* A summary of the plan must be provided to your employees.

Simplified employee pension plans: An IRA simplified employee pension plan is a written retirement plan that allows an employer to contribute directly to an IRA account for his or her employee(s). Your own contribution as an employer is made on the basis of a percentage of your income; additionally, you must contribute the same percentage of income for each employee that you contribute for yourself.

Contributions must be made for all employees who are over the age of 21, who have worked for you for at least three out of the past five years, and who have received at least $385 in wages in the calendar year. Contributions must also be made for all employees who have met the eligibility requirements, even if they terminated employment during the year.

You are not required to contribute every year and, unlike a Keogh plan, a simplified employee pension plan can be established after the end of the tax year.

Conclusion

For investors, the scope of investment options is broad, ranging from conservative savings accounts and savings bonds to the considerably more risky mutual funds and stocks.

By knowing your individual financial goals and the extent to which you wish to "gamble" your discretionary income, you can select investment options more easily and confidently. Remember, however, that understanding the risk and reward attributes of each investment option is essential when choosing among various alternatives.

This article is designed to introduce the reader to the range of investment opportunities and to provide basic information regarding their advantages and disadvantages. Several information sources, including books, magazines, accountants, and financial advisors, should be consulted when making investment decisions. Remember that financial planning, like most long-term decisions, requires thoughtful, complete, and objective consideration; your choices affect the success of your financial future! Good luck!

References available upon request

[TABULAR DATA OMITTED]

Table 3

ITEMS TO CONSIDER WITH YOUR FINANCIAL ADVISOR

* What type of fees (direct or indirect) are associated with your investments?
* How quickly can you access your money?
* Is there a penalty or fee associated with accessing your money?
* How much risk is associated with your investment?
* Is there a prospectus for the suggested investment?
* Why is the particular investment suggested?
* How does the recommended investment meet your needs and goals?
* What is the possibility that you will lose all or part of your money?

Table 4

THE VANGUARD GROUP HIGH YIELD CORP. BOND FUND PORTFOLIO HOLDINGS -- JULY 31, 1993

Industry	Company
Consumer goods	Dr. Pepper Bottir
	Fruit of the Loom
	Sealy Corp.
Grocery stores	Kroger Co.
	Safeway Inc.
	Stop and Shop

Media & communications	McCaw Cellular Turner Viacorn Internatie
Retail stores	Ann Taylor Inc. Levitz Furniture Payless Cashway
Food and lodging	ARA Group Marriott Corp. Flagstar Corp.

Table 5

INFORMATION RESOURCES

Money market accounts Savings accounts Credit unions	Local financial institutions Banks Savings and loans
United States savings bonds Treasury bills	Government publications Public Affairs Office, U.S. Savings Bonds Division Department of the Treasury Washington, DC 20226
Mutual Funds	Money Forbes U.S. News & World Report Morningstar Inc.
Stocks	The Wall Street Journal Brokers

OBJECTIVES:

This lesson, good for two CE credits, requires a passing grade of 70%. Upon completion of this article, the pharmacist should be able to:

* Describe the rationale and value of financial planning
* List the steps involved in financial planning
* Differentiate the risk mere options, including stocks, mutual funds, savings bonds, and retirement accounts
* List the benefits and disadvantages of both tax-deferred and nontax-deferred investment options

GOALS:

To provide basic information regarding various components of the financial planning process and to introduce various investment options, including their advantages, disadvantages, risks, and benefits

If you are:	You can take a full deduction if your modified AGI(*) is:	You can take a partial deduction if your modified AGI is:
Single	Less than $25,00	$25,000 to $35,000
Married	Less than $40,000	$40,000 to $50,000

(*)AGI = adjusted gross income

Step one: Calculate Mary's contribution:

Mary's annual income	$50,000
Contribution percentage	10%
Total contribution in dollars	$5,000

Step two: Calculate employer's match:

Employer's matching contribution ($5,000 x 50 cent)	$2,500
Less excess over employer's cap	
Employer's contribution less the employer's	

contribution cap of 4% ($2,500 - [$50,000 x .04!) ....($500)

Total contribution for 1994 ....$7,000

An example of a typical pension plan calculation is as follows:

Average of your five highest annual salaries	$60,000
Multiplied by a fixed factor	2%
	1,200
Multiplied by the number of years of service	30
Annual pension benefit	$36,000
Monthly pension benefit	$3,000

Average of your five highest annual salaries	$63,000
Multiplied by a fixed factor	2%
	1,260
Multiplied by the number of years of service	33
Annual Pension Benefit	$41,580
Monthly Pension Benefit	$3,465

04190873 SUPPLIER NUMBER: 15998747 (THIS IS THE FULL TEXT)
Quick study: total return. (figuring out mutual fund returns)
Moreau, Dan
Kiplinger's Personal Finance Magazine, v49, n1, p111(1)
Jan, 1995

TEXT:

For figuring the gain or loss on an investment, the change in its market value is only the beginning.

How did your investments do in 1994? Did you beat the averages? (Most mutual fund managers didn't, at least not through Halloween.) Would you have been better off in certificates of deposit? (Investors in the 3,000-plus mutual funds that lost money during the first ten months of 1994 would have been.) The illustration below presents some key benchmarks against which to measure your success.

But before you can decide whether you should be strutting or skulking, you need to know how your funds really performed - which brings us to "total return."

"It's the ultimate measure," says Vanguard Group chairman John Bogle. And, on its face, it's easy to figure.

To find total return, first add together distributions, such as dividends and capital-gains distributions, you received during the year. To that figure, add (or subtract) the change in share price between the beginning and the end of the year. Divide the resulting total by the share price at the beginning of the year.

For example, say that for all of 1994 you owned shares of "Total Return **Mutual Fund**," which started the year at $6 per share. Over the course of the year, the fund paid 25 cents per share in dividend income and another 25 cents per share in **capital - gains distributions** - your share of the profits on the stock trades inside the fund. At year's end, the share price was $7. Adding the 50 cents of income to the $1 of appreciation gives you $1.50. Dividing that by the beginning-of-the-year value of $6 indicates an enviable total return of 25%. That is not, however, what you'd hear if you asked the fund for its 1994 total return. Funds give you a slightly higher figure because the simple formula above assumes you take your dividends in cash. When a fund figures total return with the help of a **computer**, it assumes dividends are reinvested, so the return gets a boost from compounding. Note, too, that if you're in a load fund, the total-return **calculation** ignores the sales charge you paid to buy shares.

If you bought into a fund during 1994 or purchased or redeemed shares during the past year, your personal total return might bear little resemblance to the official 1994 numbers. Because share prices fluctuate, when you buy can make a lot of difference. To get a better idea of how the fund did while you owned it, check the Wall Street Journal. On Wednesdays, Thursdays and Fridays, the paper reports fund returns for the previous three, six and nine months, respectively. If you bought or sold shares during the year, you'll need a financial calculator or computer program to figure your true total return. In the near future, though, some funds may have software to produce such a personalized total return.

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The Taming Of The Code

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ABSTRACT: Three rules of thumb for taming the tax code are: 1. You would rather have a long gain than a short one. 2. You would rather have a short loss than a long one. 3. The best thing of all is a gain you never realize.

TEXT: LONG ISLAND, N.Y. RESIDENT Rosanne Guinan, 77, majored in math at Cornell, works as a mainframe systems programmer and has long tracked her investments on a spreadsheet. In her taxable accounts, she owns mostly stocks, rather than funds, so she can control when she recognizes capital gains. Yet even tax-savvy Guinan would sometimes accidentally sell a stock before the one-year-and-a-day holding period for the long-term-gains rate was met.

But now she is using www.gainskeeper.com, a service that allows her to see all her gains and losses instantly, displayed in separate columns depending on whether they're short-or long-term. "It gives me a picture that isn't available from my little spreadsheet," she says.

Personal-finance software and the Web are helping do-it- yourselfers tame the tax code. No, you still can't buy cheap off-the-shelf software that will allocate all your investments tax-efficiently. But you can track your gains and actively "harvest" losses--realize them, that is, in time to get a tax benefit from them--just the way the pros do.

Three rules of thumb: (1) You'd rather have a long gain than a short one. (2) You'd rather have a short loss than a long one. (3) The best thing of all is a gain you never realize. Buy Home Depot at $1 a share, hang on until you donate it to charity or bequeath it, and the capital gain is never taxed.

That's the theory. How do you get the results? Technology is helping. It is making possible cheap alternatives to those fed up with the costs and hidden tax bombs of mutual funds.

FORBES columnist Peter Huber predicted this more than a year ago, (see FORBES, Feb. 8, 1999); what he talked about in a hypothetical way is now reality. Got $100,000 in investment assets? American Express will allow you to make free online trades of up to 3,000 shares each, so long as you keep that much in an account and don't engage in "excessive trading." AmEx makes its money on margin loans and by selling you other products--mutual funds, insurance, charge cards and financial planning.

If you know what you are doing, you can run your own personal **mutual fund** without the overhead or tax problems of a fund. Remember, even a tax-efficient **mutual fund** can do only so much for you at tax time. It can avoid selling winners, letting them compound tax-free, but it cannot sell losers in such a way as to put the write-offs on your Schedule D. Funds flow through net gains to their customers but cannot do the same for net losses. Then there's Foliofn.com, an intriguing new service launched

in May by former SEC commissioner Steven Wallman. For a flat $295 a year investors can maintain three "folios" with up to 50 stocks in each. You can build your own special portfolio or pick from dozens of prepackaged ones designed to mimic a stock index or a style (say large cap, or value), a sector or a certain level of risk. The key is that investors who use dollar-cost averaging can put in their $100 or $1,000 a month--just as they might make contributions to a **mutual fund** --and the money will be spread evenly over the folio, including into fractional shares. Meanwhile, the service **tracks** an **investor** 's taxable **basis** in each stock separately.

So, for example, you could (at no extra cost) sell shares of a losing stock, realize the loss and replace it in the folio with a comparable security, while maintaining your target diversification and risk level. Hold your substitute stock for 31 days to avoid the "wash sale" rule, and then you can switch back into the original security.

(This service isn't for day traders, since the basic fee allows you to trade at only two preset times each day. At all other times, you pay $15 a trade.)

It was always possible for people with $10 million to do this sort of thing. Now the $100,000 crowd can participate, too.
THIS IS THE FULL-TEXT.

00384483 88-01316
Fidelity Lauds Stratus' Faithful Computing
Nichols, Paula
Wall Street Computer Review v5n2 PP: 52-58 Nov 1987 ISSN: 0738-4343
JRNL CODE: WSC
DOC TYPE: Journal article LANGUAGE: English LENGTH: 5 Pages

ABSTRACT: Fidelity Systems Co., the data processing subsidiary of Fidelity Investments, uses systems from Stratus **Computer** to provide fault-tolerance processing as part of its end-of-day **mutual funds** pricing. The online transaction processing allows thousands of customer requests to be handled daily. Necessary market information from several quotation services is received, and the net asset value of all of Fidelity's **mutual funds** is **calculated** by the end of the business day to be published in the next morning's financial listings. Through the use of Fidelity Investor's Express (FIX) personal **computer** service, investors can price their portfolios, inquire about prices, or buy and sell stocks or **mutual funds** . The Fidelity Automated Service Telephone (FAST) supplies over 12,000 quotes to shareholders a day. Fidelity's Stratus XA2000 has allowed the company to expand the price database and develop complex applications.

DIALOG(R)File 275:Gale Group Computer DB(TM)

01443341 SUPPLIER NUMBER: 11039445 (THIS IS THE FULL TEXT)
Fidelity's formula: technology keeps customers happy. (Fidelity Investments; includes related article on use of various technologies in customer service)
Schwartzman, Sharon
Wall Street Computer Review, v8, n10, p27(4)
July, 1991

TEXT:

At one of Fidelity Investments's four customer service phone centers, located in Boston's flag-bedecked World Trade Center, the quantity of time a phone rep spends with a customer is going down while the quality of service provided is rising. This more-for-less approach is integral to the company's goal of staying on the leading edge.

Fidelity, the Boston-based, privately held, financial services firm and mutual fund success story, enthusiastically strives to meet this goal. The firm aims to use technology to achieve better customer service, add new products and services and reduce expenses. Fidelity is currently rolling out new workstations for its phone reps to give better quality customer service. It is also loading new technologies, such as imaging and electronic proxy voting, into its arsenal, part of an ongoing process to improve service while reducing cost.

Fidelity deploys technology extensively, with a firmwide technology staff of over 850 who work in a structure both centralized and decentralized. The central group sifts out the technologies, says Albert Aiello, Jr., chief information officer of Fidelity Investments and president of Fidelity Systems Co., a division of FMR Co. (the shortened version of Fidelity Management and Research Co.), while the others work continuously with user requirements. The two combine forces to actualize projects.

Fidelity spends more than $150 million a year in the technology area. "We couldn't have grown without the technology," says Laurence J. Dwyer, director national news, "but we wouldn't have needed as much technology if we hadn't grown. We have six million customer accounts, and we need the technology to reach those people."

As it has invested in high-tech, Fidelity's assets under management have mushroomed. The firm, begun in 1946, had roughly $ 10 billion under management in 1980, says Dwyer, $25 billion in 1985, $118 billion in 1990 and now happily manages $137 billion. Over the past decade, Fidelity has invested hundreds of millions of dollars in technology.

The Secret of Success. Fidelity's success entails mingling the right approach with the right products. "The fund business is very much customer driven these days," says John Keefe, an analyst with Lipper Analytical Securities, New York. Until the crash in 1987, he says, the customer was happy to buy anything that came along, since the markets were all rising. Toward the end of the decade, though, people became more cautious and more appreciative of risk. Fund companies found they are better off trying to cross-sell and sell additional products to the existing customer base rather than chase new business. They've accomplished this by enhancing the service relationship, Keefe says.

William Gruber, president of Research & Planning, an information technology consulting company based in Cambridge, Mass., agrees, saying that the key is having the right business vision. There has been a shift away from the old traditional broker with high-priced registered reps, he says, to the new traditional broker with massive technology-supported customer service--a shift from a selling mode of marketing to a customer-support mode facilitated by technology. "Fidelity is probing its technology, and having seen a competitive advantage, it keeps improving on that," says Gruber.

In addition, Fidelity "has been in the right place at the right time with products," Keefe says. A prime example is the Magellan Fund, "which was really a badge of authority for Fidelity." Magellan was the top performer of all long-term taxable funds for both the 15- and 10-year period ending March 31, according to Lipper Analytical Services Inc.'s

rankings. And it's got plenty of companions--192 other funds, many with their own impressive records. For the one-year period ending March 31, Fidelity's Select Biotech, Select Medical and Select Health funds were the top three performers on Lipper's list.

Fidelity's technology expenditure as a percent of sates has remained constant, though not necessarily by design. With operating revenues of $1.27 billion for 1990 (net operating income of almost $32 million), that would give technology about an eight percent slice of the pie.

The Real Payback. However, such a ratio tells only part of the story, says Gruber. In studying costs, he says, the question isn't what a firm spends, but what is the expense versus the payback, business function by business function.

Fidelity adheres to this strategy. Says Gruber: "Its productivity at the customer marketing and support level, which is highly computerized, says it is getting a high payback." Spending, says Aiello, "is in proportion to the importance of the technology to fulfilling the company's mission." For example, the firm has over 250 Sun Unix workstations in its research and trading area. At the customer service phone centers, there are over 300 IBM clone workstations employed in various capacities. "It's balanced," Aiello says. "We're not skewed in any direction."

Still, the firm sees customer service as its lifeblood for this decade. "We feel service is the competitive front of the 1990s," says Aiello. We've got to provide the best service if we're going to keep our customers satisfied."

Customer satisfaction played a major role in the creation of the Branch Office Delivery System (BODS) and mutual fund workstation. About 25 percent rolled out with 250 workstations, the new machines can sew together extensive amounts of information from various sources, says Stephen A. Campbell, vice president, Fidelity Software Development Co. The available data ranges from customer information to quotes and news, bringing it all to the rep's fingertips within seconds. A rep can also do through the system the kinds of computations a customer may request, involving, for example, margin calculations and options analytics.

Customized Service. One desktop unit can monitor 20 securities at a time, says Campbell, zeroing in on one of those securities if a customer asks for a quote, and the system can give an expanded view of that security, including its current price, what it opened at and its dividend rate. If there is news on a security, a rep can click on a part of the screen, bring up 90 days of headlines, hone in on one, bring up the entire text and read it to a customer. Reps can also call up another screen that allows them to enter brokerage transactions. Product information is accessible as well.

The system has three components--six Stratus computers that collect real-time data from around the world, a distribution network to disseminate the information and the desktop unit. The cost of a workstation, without amortizing the first two components, Campbell says, is $4,000, an initial capital outlay that is quickly recaptured, since it is replacing terminals leased from Automatic Data Processing Inc. (ADP) and Quotron Systems Inc. The real benefit, though, is that the firm can control the information delivered to the brokerage rep, making it more versatile and focused on customer needs. Ultimately, he says, "customers can obtain information faster and more accurately."

One Fidelity phone rep, Scan Cooper, testifies to the efficiency of the system. He says that in the past he would have to put a customer on hold for minutes at a time to check, for example, a customer's mutual fund holdings or to retrieve a news story. These functions are now accomplished within seconds. **Computer calculations** replace paper and pens, which also cuts down on time and errors. Before, he used an ADP terminal, which was not as complete, he says. For instance, ADP would give a stock symbol where BODS also gives the stock name and cusip number, helping to avoid confusion in dealing with stocks with similar names. "I had an IBM 3191 terminal with access to the brokerage system, and a separate ADP terminal for news and quotes," says Cooper. "When you compare the two systems, the current one is lightyears ahead."

The Complete Picture. The customer, though, is only half the story. The product is the other and is handled by the research, portfolio management and trading area, which has fully deployed its Sun workstations

for about a year, says Aiello. Fidelity does not try to time or predict the market, says Dwyer. Instead it researches companies' earnings growth, how they are managed, their product line, and so on. "If you pick good companies, you'll make money for your investors," he says. While Fidelity does provide money management systems, there is no core analytical processing piece.

Magellan's former portfolio manager, Peter Lynch, was a highly visible example of a Fidelity money manager, and he believed in grassroots research of companies. In his book, One Up on Wall Street, Lynch writes that his studies of quantitative analysis at Wharton, "taught me that the things I saw happening at Fidelity couldn't be happening." This skepticism notwithstanding, Fidelity has invested substantially in systems technology for securities trading and management. Its order management system for equities and fixed-income trading evolved in the mid-1980s. The firm started its Sun rollout in 1987. The latest step is the InView workstation, which cost more than a million dollars and was three years in the making, under the direction of FMR Co.'s Kathy Eklund, director of systems, and Chuck Dornbush, chief financial officer of mutual funds. InView is designed to deliver on one screen information from Wall Street, external news, market data, research services and Fidelity's internal research and analysis. One of its services is a market-watch screen, from Bridge Information Systems, which highlights price changes and flags stocks as they hit their highs and lows each day. Another offering is Thomson Financial Services's First Call, which offers real-time stock information. With View Notes, a user can gain access to Fidelity analysts' daily notes on companies from an on-line database that stores 18 months of reports. The rollout to portfolio managers, whom Aiello estimates total about 70, should be complete by midsummer.

Brad Lewis, portfolio manager of the Fidelity Disciplined Equity Fund and Stock Selector Portfolio, combines InView with his proprietary stock valuation model, which uses artificial intelligence and was built in DOS on a Gateway 33-megahertz 486 computer. His model reconciles stock price with, for example, earnings, earnings growth, financial leverage and company size. "You kind of back into what the stock price should be based on how the market currently is valuing stocks overall," he says.

He manages each fund differently. The Disciplined Equity Fund, with $137 million in assets, involves only stock picking, and Lewis diversifies in the same way the industry does--if food stocks are three percent of the S&P, they will be three percent of the fund. Stock Selector, with $88 million, has 40 econometric models that forecast industry returns, which he overlays with the individual stock picking of the Disciplined Equity Fund to tilt toward individual sectors.

Quality Assurance. So what role does InView play? "You've got to be careful with any quantitative investment style," says Lewis, "in that you can have garbage in, garbage out." He uses InView for what he terms "quality assurance"--for instance, checking news headlines that may not be accounted for in the models. With his models, he says, he can assimilate huge amounts of information quickly and objectively, "much more so than I could qualitatively myself" With InView, Lewis can check short-term fundamentals quickly, "rather than running around to the analysts or going to the library." The combination has proven itself One goal of Disciplined Equity is to beat the market; in 1989 and 1990 it did, and so far it is ahead this year, too. Since it started in December 1988, it's up 63.6 percent, Lewis says. Begun last September, Stock Selector is up 29 percent year to date versus 15.8 for the S&P.

Lewis quickly points out, however, that his system is not a black box that just looks at technical stock patterns. It assimilates a great deal of fundamental data. He does admit that while most Fidelity fund managers go out and talk to companies or use analysts' recommendations for stock ideas, his source is the computer combined with looking at fundamental data.

"Quantitative methods in portfolio measurement is the single area that comes to mind where Fidelity falls short," says Gruber of research & Planning, admitting a bias toward quantitative techniques. But funds like Magellan, he says, are examples that a firm can still win with qualitative research.

The future, Aiello says, promises more customer service technology and lowering costs through technology. Customer support, he continues, is

what the customer considers good service, which evolves over time. "Customer demands may be this today and that tomorrow. Technology has to be flexible enough to incorporate change. I plan for that in ways that allow me to have flexibility in the technologies I bring to bear."

Customer-driven businesses are the way of the future, and as a prime example of one, Gruber says, "Fidelity deserves an A++."

The Many Opportunities in High-tech Customer Service

Other customer-service-oriented technologies under way at Fidelity include imaging, printing and electronic proxy voting.

Plan I: Using a systems integrator and a variety of vendors, Fidelity aims by mid-summer to image checks and slice out the payee information, payee detail and amount, sending a customer with mutual fund checking an imaged statement. It con also be sorted by type of expenditure, using an expense code.

Payoff: "Customers have got one or two pieces of paper with all the images on it, if they prefer, rather than a box full of checks," says Albert Aiello, Fidelity CIO. "At the end of the year, you can scan that to find, say, Did I ever pay the plumber? You would look at 12 or 15 pages as opposed to going through hundreds of checks to find the plumber."

Internally, this technology opens up other cost-saving possibilities. For example, in back-office applications, if a customer calls to ask whether a payment has been received, the check could be pulled up on screen. Customer letters con be captured as well, simplifying record keeping.

Plan II: Fidelity is also working on its penmanship, improving its printing capabilities for individual and institutional customers. For instance, in handling companies' 401k's, the firm is fine tuning the printing of company logos on reports, duplicating down to the finest detail the logo Of, say, the Showboat Hotel in Atlantic City.

Payoff: Customers are more satisfied with the qualify of documents they present to, for example, their employees.

Plan III: Another development involves an innovation in an area long ignored--proxy voting. As an institutional investor, Fidelity holds stock in probably 2,500 companies, says Poul L. Ciriello, general manager of Proxy Edge, a service that offers record keeping software and an electronic voting system for use by both Fidelity as well as outside customers.

Payoff: Replying to companies' proxies means Fidelity must process 30,000 to 40,000 pieces of mail, says Ciriello, since each company sends a ballot to Fidelity for every Fidelity portfolio that holds its stock. With Proxy Edge, electronic ballots replace paper, allowing for automatic tracking of voting activity, which saves time and money.

Bonus Payoff: The product has been released to 50 customers, says Ciriello, including banks, public and corporate pension plans and other investment advisers. "A couple of banks in New York indicated to us that they could save as much as $150,000 a year," he says. Proxy Edge is priced either as a function of equity assets under management, a sliding scale, or on a transaction basis. It ranges from $7,500 to $15,000 per year.--S.S.

An overview of limited liability companies

Ward, J Marc. **The Practical Real Estate Lawyer**. Philadelphia: Mar 1993. Vol. 9, Iss. 2; pg. 61

Subjects:	Revenue procedures & rulings, Rev. Rul. 89-12, Rev. Rul. 88-76, **Real estate**, **Limited liability companies**, Investments, Definitions, Advantages
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Abstract (Article Summary)

Limited liability companies (LLC) offer an ideal alternative to the other forms of business entities for real estate investments. Their unique cross-section of corporate and partnership characteristics are ideally suited for many real estate investments. Limited liability companies may become the dominant form for doing business in the near future. Eighteen states now permit limited liability companies to be organized, and every other state in the union, except for Arkansas, has shown interest in LLC legislation. Real estate investors looking for the single-tax benefits of S corporations without the many complications that accompany that status and who also want the limited liability protections of corporations that are not available to partnerships should seriously consider LLCs.

Full Text (4264 words)

Imagine a general partnership where all of the partners have the limited liability of shareholders and the tax treatment of a partnership.

The limited liability company, a recent innovation in business law, is just such an entity. These companies have the tax characteristics of partnerships with the limited liability aspects of corporations for all investors (called members). Eighteen states now permit limited liability companies ("LLCs") to be organized, and every other state in the union save Arkansas has shown interest in LLC legislation.

THE DEBUT OF THE LLC * Although LLCs have been common abroad for many years, it was not until 1977 that Wyoming adopted the first limited liability company act in the United States. The Wyoming act was special legislation for a Texas mineral concern. Florida followed suit in 1982 on the assumption that Latin American LLCs might be encouraged to do business in Florida. Businesspersons were reluctant to use an LLC, however, until its tax status was resolved.

TAX STATUS OF LLCs

In 1988 the Internal Revenue Service ("IRS") ruled on the tax status of LLCs. In Revenue Ruling 88-76, 1988-2 C.B. 360, the IRS concluded that LLCs would be taxed as partnerships so long as they failed two of the four key tests that distinguish partnerships from associations. Failing these tests is the sine qua non of LLCs, but also represents the two important drawbacks to such entities, as discussed later in this article.

This article will explain some of the key terms you need to know when working with LLCs, highlight the advantages LLCs have over S corporations and partnerships, describe how LLCs are created and reorganized, discuss the essential attributes LLCs must have to be taxed as partnerships, and review some other key issues involving LLCs.

BASIC VOCABULARY

As with other business entities, LLC statutes have adopted a unique vocabulary. Here is a glossary:

ARTICLES OF ORGANIZATION

The articles of organization is the document filed under the act for the purpose of forming an LLC.

CAPITAL CONTRIBUTION

A "contribution" to an LLC can include cash, property, or services rendered, or a promissory note or other binding obligation to contribute cash or property or to perform services, that a member contributes to an LLC in the capacity of a member.

LIMITED LIABILITY COMPANY

A limited liability company is an entity that is an unincorporated association with two or more members organized under the applicable state statute. Thus, by definition, an LLC is an unincorporated association, and must have at least two members. The Texas LLC act permits LLCs to have one member, but the tax status of such an entity is open to question.

MANAGER OR MANGERS

Manager or managers refers to a person or persons designated by the members of an LLC to manage the LLC as provided in the articles of organization or an operating agreement.

Member

A person that owns an interest in a limited liability company is a member.

MEMBERSHIP INTEREST OR INTEREST

A member's share of the profits and losses of the LLC and the right to receive distributions of the LLC's assets is an interest or membership interest in the LLC.

OPERATING AGREEMENT

An agreement of members of an LLC on the affairs of the LLC and the conduct of its business is an operating agreement. An operating agreement can be written or oral.

ADVANTAGES OF LLCS OVER S CORPORATIONS AND PARTNERSHIPS * LLCs have the advantages of S corporations and partnerships without the disadvantages inherent in both.

ADVANTAGES OVER S CORPORATION

LLCs and S corporations provide limited liability to their owners and the pass-through of income and loss to them. However, LLCs have the following advantages over S corporations.

ANY PERSON OR ENTITY

Any type of entity or person can be a member of an LLC, including entities that are prohibited from owning stock in an S corporation, such as a:

* Corporation;

* Partnership;

* Nonresident alien;

* Employee Stock Ownership Plan ("ESOP"); or

* Charity.

Internal Revenue Code ("IRC") Secs 1361(b)(1)(B), 1361(c)(2).

UNLIMITED NUMBER OF MEMBERS

An LLC may have an unlimited number of members, while an S corporation is limited to no more than 35 shareholders. IRC Sec 1361(b)(1)(A).

DISPROPORTIONATE DISTRIBUTIONS

An LLC may make disproportionate distributions and allocations among its members, but an S corporation is limited to a single class of stock that makes special distributions of cash flows or allocations of income or loss not possible. IRC Secs 1361(b)(1)(1)(D), 1377 (a)(1).

LIABILITIES INCREASE BASIS

An LLC's liabilities can increase the basis of the members in their LLC interests. The liabilities incurred by an S corporation do not increase the "outside basis" of the shareholders' stock. Rev. Rul. 71-288, 1971-2 C.B. 319.

NO GAIN ON DISTRIBUTION OF APPRECIATED PROPERTY

LLCs will not recognize gain on the distribution of appreciated property, however, S corporations will recognize gain upon the distribution of appreciated property. IRC Sec 311(b).

NO INADVERTENT LOSS OF PASS-THROUGH STATUS

LLCs cannot inadvertently lose their pass-through tax status, as can an S corporation.

CONTRIBUTIONS OF APPRECIATED PROPERTY

Unlike an S corporation shareholder, a member of an LLC is allowed to contribute appreciated property to an LLC in exchange for a membership interest without having to recognize gain on the transfer regardless of whether the member owns 80 per cent or more of the LLC.

TAX ADVANTAGES OF PARTNERSHIPS

LLCs share the same tax advantages found in partnerships. LLCs, like general and limited partnerships (and S corporations), have pass-through tax advantages so the only tax is at the investor level. Because they are taxed as partnerships, members of LLCs also enjoy such tax advantages as increased basis adjustments for company liabilities and stepped-up basis in its assets upon the sale or transfer of a membership interest. LLCs can also allocate income and tax liabilities freely among their members, just like a partnership, to fit the members' needs.

ADVANTAGES OVER PARTNERSHIPS

In addition, LLCs have significant advantages over general and limited partnerships.

LIMITED LIABILITY

All members of an LLC have the benefit of limited liability regardless of their involvement in the management of the company. No member of an LLC is liable for the debts of the company.

ACTIVE PARTICIPATION IN MANAGEMENT PERMITTED

Limited partners in a limited partnership run the risk of losing their limited liability status if they become too involved in the business of the partnership. The ability of investors in an LLC to actively participate in management without losing their limited liability status may also permit those members to convert what are known as "passive" tax losses to "active" tax losses that could have a favorable tax result for those members.

NO NEED FOR GENERAL PARTNER

Moreover, using an LLC instead of a limited partnership avoids the need for a general partner and, in the case of a corporate general partner, compliance with the IRS requirements. Rev. Proc. 89-12, 1989-1 C.B. 798.

CREATION AND ORGANIZATION * LLCs are created by filing articles of organization with the secretary of state.

ARTICLES OF ORGANIZATION

The articles of organization in most states merely require:

* The name of the LLC (with the words "Limited Company" or the abbreviation "L.C.");

* Its period of duration, which cannot be perpetual (some states limit the duration to 30 years);

* The name and address of the registered agent; and

* The name and address of the LLC's principal office.

OPERATING AGREEMENT

In addition to its articles of organization, an LLC may have an operating agreement. The operating agreement is similar to a partnership agreement or corporate bylaws. It contains provisions for:

* The management of the LLC;

* The election of its managers;

* Capital contributions; and

* The allocation of profits and loss among its members.

Unlike limited partnerships, most states do not require a filing of a certificate identifying the members and their capital contributions. See the Appendix for an outline of a typical operating agreement.

MANAGEMENT PROVISIONS

The owners, or members, may participate directly in the LLC's management or the management of its business may be vested in one or more managers. Managers are elected, like the directors and officers of a business corporation. If all of the members are entitled to manage the business, any member can bind the LLC in dealing with third parties unless specifically limited in the articles of organization.

TWO-MEMBER REQUIREMENT

An LLC, because it is intended to be taxed as a partnership, must always have at least two members. For that reason, the definition of limited liability company contained in most LLC acts requires that an LLC have at least two members. It is essential that the LLC already have at least two initial members at the moment it comes into existence. To protect an LLC's partnership tax status and as preparation for any future due diligence review of the LLC's records, a document should be created evidencing the LLC's initial membership.

STATE LAW AND TAX LAW

This concept of two members is an important point from both a state law and a tax law standpoint. From the perspective of state law, an entity is not an LLC unless it has two members at all times. When structuring an LLC, the tax implications of the identity of the members is critical. For instance, for tax purposes a husband and wife can be partners (Rev. Rul. 77-332, 1977-2 C.B. 484 and Rev. Rul. 58-243, 1958-1 C.B. 255). But it is very risky to set up a shell corporation to act as one's other member in light of the single economic interest theory. See Rev. Rul. 77-214, 1977-1 C.B. 408 (a German LLC, a GmbH, was taxable as a corporation because its two members were subsidiaries of the same U.S. parent); But see Rev. Rul. 75-19, 1975-1 C.B. 382 (a general partnership composed of four corporate partners, all wholly owned subsidiaries of a domestic corporation, was a partnership for tax purposes) and Pvt. Letter Rul. 92-39-014 (husband and wife each was a limited partner and the general partner was a corporation owned by the husband. IRS ruled that the limited partnership would be taxed as a partnership).

MANAGEMENT OF AN LLC: MEMBER OR MANAGER?

An LLC may be managed either by its members, or by a manager or managers elected by the members. If an LLC is to be manager-managed, the articles of organization or an operating agreement must specify this choice. If not specified, the LLC will be deemed to be member-managed in most states.

The manager form offers tremendous flexibility in structuring the operation of an LLC. An operating agreement (or the articles of organization) could implement a variety of alternatives involving the responsibilities and voting power of managers. It has been suggested that under some circumstances, organizers might wish to set up two managerial classes that would be equivalent to the functions of corporate officers and directors. In most states a manager can be any person, including a corporation.

NUMBER, ELECTION, AND REMOVAL

The number of managers is fixed by or in the manner provided by the articles or an operating agreement, and is subject to amendment. Managers are elected, and vacancies among managers are filled, by a vote of members. Managers may be removed in the manner provided in the articles or an operating agreement, and if no such provision is made, most states provide that they may be removed with or without cause by a majority vote of the members.

CLASSIFICATION OF AN LLC AS A PARTNERSHIP FOR TAX PURPOSES * IRS regulations provide that a corporation has a number of characteristics that distinguish it from other organizations.

THE DISTINGUISHING CHARACTERISTICS OF A CORPORATION

For tax purposes the distinguishing characteristics of a corporation are:

* Associates;

* An objective to carry on business for profit;

* Continuity of life;

* Centralized management;

* Limited liability; and

* Free transferability of ownership interests. Treas. Reg. Sec 301.7701-2(A)(1). See Morrissey v. Commissioner, 296 U.S. 344 (1935).

An "unincorporated organization" will not be classified as an association for tax purposes unless it has more corporate characteristics than noncorporate characteristics, excluding characteristics that are common to both partnerships and corporations. Treas. Reg. Sec 301.7701-2(a)(3). The characteristics of having associates and a profit objective are common in both partnerships and corporations and are thus disregarded. Since LLCs should always have limited liability, the key tests are continuity of life, free transferability of membership interests, and, to a lesser extent, centralized management.

CONTINUITY OF LIFE

The IRS regulations provide that a limited partnership does not have continuity of life if the death, retirement, or insanity of a general partner causes the dissolution of the organization, unless the remaining general partners agree to continue the partnership or all of the remaining members agree to continue the partnership. Treas. Reg. Sec 301.7701-2(6)(1). The IRS regulations do not address by name limited liability companies. However, in Rev. Rul. 88-76 the IRS ruled that for federal income tax purposes a Wyoming LLC would be taxed as a partnership. Rev. Rul. 8876, 1988-2 C.B. 360. The Wyoming LLC act required that an LLC would dissolve upon the death, retirement, resignation, expulsion, bankruptcy, or dissolution of a member unless the business of the LLC is continued by the consent of all of the remaining members. Based on this provision the IRS concluded that the LLC lacked continuity of life.

ASSURING LACK OF CONTINUITY OF LIFE

As a result of this ruling most professionals concluded that to assure that an LLC lacked continuity of life the LLC had to dissolve upon the happening of a triggering event unless the unanimous consent of the remaining members was obtained to continue the business. Some LLC acts mandate this treatment ("bullet-proof" statutes) while others permit the organizers to determine whether the LLC will have this attribute or perhaps a lower threshold for continuing the business, such as majority consent of the remaining

members ("flexible" statutes). The most cautious observers suggested that the provision in the Wyoming act that limited the life of an LLC to a maximum of 30 years was also necessary to assure the lack of continuity of life even though this provision was never mentioned by the IRS in Rev. Rul. 88-76.

BANKRUPTCY OF ONE PARTICULAR MEMBER

Recently, the IRS has relaxed this stringent standard of unanimity. In Pvt. Letter Rul. 92-10-019 (Dec. 6, 1991), the operating agreement of a Texas LLC provided that if M, the corporate member/manager, ever went bankrupt, the LLC would dissolve unless all of the remaining members agreed to continue the business. The IRS found that this LLC lacked continuity of life even though the triggering event was limited to one type of event (bankruptcy) occurring to one pre-identified member (the corporate manager). If the corporate manager was simply a shell operating entity, this LLC has an almost unlimited life expectancy, subject only to the period of duration listed in the articles of organization.

ALL OF EXECUTIVE COMMITTEE, MAJORITY OF MEMBERS

In Pvt. Letter Rul. 92-26-035 (Mar. 26, 1992), the operating agreement of a Utah LLC provided that the LLC would dissolve upon the death, retirement, resignation, expulsion, bankruptcy, or dissolution of any member unless all of the member/managers on the executive committee and a majority of the other members (in number and voting interest) agreed to continue the business of the LLC. The IRS concluded that this LLC lacked continuity of life. Note the parallel to limited partnerships in Treas. Reg. Sec 301.7701-2(b)(1).

MAJORITY OF PARTNERS

The IRS disclosed in Rev. Proc. 9235, 1992-18 I.R.B. 21, that it would not take the position that a partnership has continuity of life if under local law and the partnership agreement the bankruptcy or removal of a general partner causes dissolution unless the remaining general partners or at least a majority of the remaining partners agree to continue the partnership.

PROPOSED AMENDMENT

On July 22, 1992, the IRS announced a proposed amendment to the section 7701 regulations that would lower the standard for determining whether a limited partnership possessed continuity of life from unanimous consent to at least majority consent. Prop. Treas. Reg. Sec 301.7701-2(b)(1).

LESS THAN UNANIMITY RISK

Lowering a dissolution vote to something less than unanimous is not without risk. See Pvt. Letter Rul. 90-10-027 (Dec. 7, 1989) (LLC possessed continuity of life when majority consent continued the entity); Pvt. Letter Rul. 90-35-041 (June 1, 1990) (withdrawing Pvt. Letter Rul. 90-10-028 (Dec. 7, 1989), which had allowed 85 per cent consent).

FREE TRANSFERABILITY OF MEMBERSHIP

The IRS regulations provide that free transferability exists if each member or those members owning substantially all of the interests in the organization have the power to substitute for themselves a person who is not a member without the consent of the other members. Treas. Reg. Sec 301.7701-2(e). The characteristic does not exist if a member can, without the consent of other members, only assign his right to share in the profits, but cannot assign his rights to participate in the management of the organization. Id.

UNANIMITY REQUIREMENT

In Rev. Rul. 88-76, 1988-2 C.B. 360, the IRS found that the characteristic of free transferability of membership interest did not exist for the Wyoming LLC because the Wyoming LLC Act and the LLC's operating agreement required unanimous consent of the members to admit a substitute member into the organization, although no consent was required to transfer a right to profits. This unanimous consent requirement became the standard even though the regulations speak of "consent of other members," not "the members" or "all members."

UNIMITY REQUIREMENT ERODING

Like recent rulings on continuity of life, the IRS has recently chipped away at this perceived requirement of unanimity. Majority consent has been permitted in two private letter rulings concerning LLCs. See Pvt. Letter Ruls. 92-10-019 (Dec. 6, 1991) and 92-19-022 (Feb. 6, 1992). Consent of only a manager was permitted in Pvt. Letter Rul. 2-10-019. This is similar to a limited partnership in which only the consent of the general partner is necessary. Treas. Reg. Sec 301.7701-3(b)(2) (Ex. 1). In Rev. Proc. 92-33, 1992-17

I.R.B. 28, the IRS ruled that a limited partnership will lack free transferability of ownership if more than 20 per cent of the interests are restricted. Thus, 79 per cent of an LLC's interests could be freely transferable.

Centralized Management

The Treasury Regulations define centralized management to be present if one person or more than one person, but not all of the members of the organization, have the exclusive authority to make management decisions. Treas. Reg. Sec 301.7701-2(c).

In the case of limited partnerships, the IRS looks at the extent of the ownership interest of the limited partners. If "substantially all" of the interests in the limited partnership are owned by the limited partners, centralized management does exist. Id. For ruling purposes the IRS requires the limited partners to own less than 80 per cent of the partnership or the IRS will not rule that the limited partnership lacks centralized management. See Rev. Proc. 89-12, 1989-1 C.B. 798.

Arguably, if a manager of an LLC owns 20 per cent or more of the LLC interests, the LLC should lack centralized management. However, in Rev. Rul. 88-76, 1988-2 C.B. 360, the IRS ruled that the Wyoming LLC in which three of its 25 members were managers had the corporate characteristic of centralized management. No mention was made of the member/managers' ownership interests.

THE INAPPLICABILITY OF REV. PROC. 89-12

Revenue procedure 89-12 set out the conditions under which the IRS will rule on whether an entity is taxable as a partnership. This revenue procedure applies to limited partnerships as well as other organizations wishing to be taxed as a partnership. Most private letter rulings concerning LLCs provide that "this ruling is subject to the requirements of Rev. Proc. 89-12, 1989-1 C.B. 798, to the extent applicable. If the requirements of Rev. Proc. 89-12 fail to be met at any time, this ruling will be void." This admonition is absent from recent Pvt. Letter Ruls. 90-52-039 (Oct. 2, 1990), 92-10-019 (Dec. 6, 1991), and 92-19-022 (Feb. 6, 1992) concerning LLCs.

LITTLE OF REVENUE PROCEDURE APPLIES

A section-by-section review of Rev. Proc. 89-12 reveals that little, if any, is applicable to LLCs. Sections 4.01 through 4.04 and 4.07 concern the economic substance of a general partner, presumably to determine whether the entity lacks limited liability. If this is the case, then the provisions should not apply to LLCs. For example, Gen. Couns. Mem. 39,798 (Oct. 18, 1989) states that the net worth requirements of section 4.07 do not apply to LLCs. Sections 4.05 and 4.06 may have some relevance to LLCs. Section 4.05 provides that the IRS will not rule that an entity lacks continuity of life if less than a majority of the limited partners can elect a general partner to replace a general partner who had been removed.

This section is not likely to apply to LLCs when the threshold is unanimity or at least majority. Section 4.06 provides that the IRS will not rule that an organization lacks centralized management if the limited partners own more than 80 per cent of the partnership. Again, this provision appears to have little applicability to LLCs.

CONCLUSION * Limited liability companies offer an ideal alternative to the other forms of business entities for real estate investments. Their unique cross-section of corporate and partnership characteristics are ideally suited for many real estate investments. Limited liability companies may become the dominant form for doing business in the near future. Real estate investors looking for the single-tax benefits of S corporations without the many complications that accompany that status and who also want the limited liability protections of corporations that are not available to partnerships should seriously consider limited liability companies.

APPENDIX

OUTLINE OF A TYPICAL LLC OPERATING AGREEMENT

1. DEFINITIONS

2. FORMATION OF COMPANY

a. Formation

b. Name

c. Principal Office

d. Registered Office and Registered Agent

e. Term

3. PURPOSE OF COMPANY

4. NAME AND ADDRESSES OF INITIAL MEMBERS

5. RIGHTS AND DUTIES OF MANAGERS

a. Management

b. Number, Initial Managers, Tenure, and Qualifications

c. Certain Power of Managers

d. Indemnification of Managers

e. Resignation

f. Removal

g. Vacancies

h. Salaries

i. Officers

6. RIGHTS AND OBLIGATIONS OF MEMBERS

a. Limitation of Liability

b. Books and Records

c. Priority and Return of Capital

d. Withdrawal of a Member

e. Actions Requiring Member Approval

7. MEETINGS OF MEMBERS

a. Meetings

b. Place of Meetings

c. Notice of Meetings

d. Meeting of all Members

e. Record Date

f. Quorum

g. Manner of Acting

h. Proxies

i. Auction by Members Without a Meeting/Telephonic Meetings

j. Waiver of Notice

8. CONTRIBUTIONS TO THE COMPANY, CAPITAL UNITS, AND CAPITAL ACCOUNTS

a. Capital Contributions

b. Capital Units

c. Capital Accounts

d. No Demand of Member Capital

9. ALLOCATIONS AND INCOME TAX

a. Allocations of Profits and Losses from Operations

b. Distributions

c. Limitation Upon Distributions

d. Accounting principles

e. Interest on and Return of Capital Contributions

f. Loans to Company

g. Returns and Other Elections

h. Tax Matters Member

10. TRANSFERABILITY

a. Assignment of Interest

b. Right of Assignee to Become a Member

11. ADDITIONAL AND SUBSTITUTE MEMBERS

a. Admission of New Members

b. Allocations to New Members

12. DISSOLUTION AND TERMINATION

a. Dissolution

b. Distribution of Assets Upon Dissolution

c. Articles of Dissolution

d. Winding Up

13. MISCELLANEOUS PROVISIONS

a. Notices

b. Books of Account and Records

c. Application of State Law

d. Amendments

e. Execution of Additional Instruments

f. Construction

g. Headings

h. Waivers

i. Rights and Remedies Cumulative

j. Severability

k. Heirs, Successors, and Assigns

l. Creditors

m. Counterparts

The term "association" refers to an organization whose characteristics require it to be classified for purposes of taxation as a corporation rather than as another type of organization such as a partnership or a trust. There are a number of major characteristics ordinarily found in a pure corporation which, taken together, distinguish it from other organizations. These are: (i) Associates, (ii) an objective to carry on business and divide the gains therefrom, (iii) continuity of life, (iv) centralization of management, (v) liability for corporate debts limited to corporate property, and (vi) free transferability of interests. Whether a particular organization is to be classified as an association must be determined by taking into account the presence or absence of each of these corporate characteristics. The presence or absence of these characteristics will depend upon the facts in each individual case. In addition to the major characteristics set forth in this subparagraph, other factors may be found in some cases which may be significant in classifying an organization as an association, a partnership, or a trust. An organization will be treated as an association if the corporate characteristics are such that the organization more nearly resembles a corporation than a partnership or trust. See Morrissey et al. v. Commissioner (1935), 296 U.S. 344. Treas. Reg. Sec 301.7701-2(a)(1)

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Counseling the Client on Limited Liability Companies, by Barbara C. Spudis, ALI-ABA Course Materials Journal, October 1992, p. 89

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Appendix C—Related Proceedings

None.